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A Reformed Antitrust Approach to Distributor Terminations

Thomas A. Piraino, Jr. *

I. THE CLASH BETWEEN MANUFACTURER AND DEALER INTERESTS: IS A JUDICIAL SOLUTION POSSIBLE?

The federal courts' approach to distributor terminations has generated more uncertainty and controversy than any other area of antitrust law. In recent cases the courts have been unable to effectively balance the interests of manufacturers and distributors. In 1984, in *Monsanto Co. v. Spray-Rite Service Corp.*,¹ and again in 1988, in *Business Electronics Corp. v. Sharp Electronics Corp.*,² the Supreme Court severely limited the ability of terminated distributors to prevail in antitrust cases. Indeed, under the interpretation of *Monsanto* and *Sharp* adopted by many lower federal courts, it has been nearly impossible for terminated distributors to reach a jury with an antitrust claim.³ In response, the retail industry, led by the large discount chains, mounted a campaign in Congress to overturn the decisions. In the 102d Congress, the House and Senate have each passed their own version of Bills (called the "Price Fixing Prevention Act") that would overrule *Monsanto* and *Sharp* and make it easier for terminated distributors to survive summary judgment motions in antitrust cases.⁴ With Congress tugging in

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1 465 U.S. 752 (1984).

2 485 U.S. 717 (1988).

3 See *infra* notes 84-88, 112-15 and accompanying text.

4 The Price Fixing Prevention Act of 1991, H.R. 1470, 102d Cong., 1st Sess. (1991), passed the House of Representatives on October 10, 1991. The Senate approved the Consumer Protection Against Price Fixing Act of 1991, 102d Cong., 1st Sess. (1991), on May 9, 1991. See 62 Antitrust & Trade Reg. Rep. (BNA) No. 1548, at 29 (January 16, 1992). A Conference Committee approved a compromise version of these Bills on June 18, 1992. See 62 Antitrust & Trade Reg. Rep. (BNA) No. 1571, at 841 (June 25, 1992). Similar bills were introduced in earlier sessions of Congress. A predecessor bill was passed by the House in November, 1987, in the 100th Congress, and again in the 101st Congress, in April, 1990. A similar bill was approved by the Senate Judiciary Committee in February, 1990. See Richard M. Steuer, *The Turning Points in Distribution Law*, 35 ANTI-

one direction and the federal courts in another, antitrust practitioners and business executives have become confused over the dividing line between permissible and illegal distributor terminations.

Much of the confusion in the approach of Congress and the federal courts can be traced to their inability to understand the economic consequences of distributor terminations. The economic characteristics of such terminations are, in fact, confusing because they involve both "horizontal" and "vertical" elements. The courts have traditionally viewed agreements among direct competitors as "horizontal" and those between firms at different competitive levels (for example, a supplier and its customers) as "vertical."⁵ Vertical agreements have been treated more leniently because they can be intended for purposes other than to restrict competition.⁶ However, in a distributor termination, it is often difficult to characterize the parties' conduct as horizontal or vertical. Discounters frequently claim that their termination was not effected independently by the supplier but was induced by pressure applied by full priced distributors. Such pressure typically is evidenced by complaints made to the supplier about the terminated distributor's price-cutting. The potential involvement of firms at the same competitive level as the terminated distributor complicates the antitrust analysis. In these "mixed termination" cases the outward form of the alleged conspiracy between the supplier and complaining distributors is vertical. However, when the distributors are able to induce a supplier to effect the termination of one of their competitors, the substantive competitive impact of the parties' conduct is horizontal.

This distinction between horizontal and vertical conduct is critical. Indeed, the distinction should determine the outcome of mixed termination cases. Terminations horizontally induced by competing distributors should be illegal because their only purpose and effect is to limit competition; however, terminations vertically imposed by a supplier should be upheld because they are almost always intended to promote interbrand competition.

TRUST BULL. 467, 495-96 (1990). The Justice Department has opposed each of these bills. See *id.* at 496; 62 Antitrust & Trade Reg. Rep. (BNA) No. 1548, at 29 (January 16, 1992).

5 See *Sharp*, 485 U.S. at 730; see also *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 608 (1972); *ES Dev., Inc. v. RWM Enters., Inc.*, 939 F.2d 547, 556 (8th Cir. 1991), *cert. denied*, 112 S. Ct. 1176 (1992).

6 See, e.g., *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977).

Unfortunately, in recent years most federal courts have not adopted such a substantive means of distinguishing permissible from illegal distributor terminations. Instead of considering whether a termination was carried out independently by a manufacturer or coerced by another distributor, the courts have been preoccupied with whether a termination was effected to enforce a "price" or "nonprice" vertical restraint. This distinction bears little, if any, relationship to the economic purpose or effect of a distributor termination.⁷ Many courts have recognized the illogic of the price/nonprice distinction, but unable to expressly overrule the distinction, they have attempted instead to limit the circumstances in which terminated distributors can prove resale price-fixing.⁸ The culmination of this approach in the *Monsanto* and *Sharp* cases, and in their progeny in the lower federal courts, eliminated most distributors' antitrust claims and prompted Congress to intervene on their behalf. The Price Fixing Prevention Act, however, is just as deficient as the current judicial approach. The Act continues to concentrate on the formalistic distinction between price and nonprice vertical restraints. Indeed, the Act expressly codifies the per se rule against resale price maintenance.⁹ The Act also pushes the judicial pendulum back too far in favor of terminated distributors. The Act permits terminated distributors to reach a jury on the basis of ambiguous evidence of a resale price-fixing conspiracy between a manufacturer and competitors of the terminated dealer.¹⁰ The conspiracy standard set forth in the Act is likely to deter manufacturers from effecting terminations legitimately intended to enhance their competitive efficiency.

A middle ground between the extreme approaches of Congress and certain of the federal courts is still available to the federal judiciary. This Article sets forth a theoretical basis under which the courts could concentrate on the legitimate economic

7 See *infra* notes 35-37 and accompanying text.

8 See *infra* notes 63-115 and accompanying text.

9 See 60 Antitrust & Trade Reg. Rep. (BNA) No. 1515, at 652 (May 9, 1991); 60 Antitrust & Trade Reg. Rep. (BNA) No. 1521, at 847 (June 20, 1991); 60 Antitrust & Trade Reg. Rep. (BNA), at 841 (June 25, 1992).

10 Under the Act, a manufacturer may be liable if a complaint from a competitor is the "major cause" of a decision to terminate a distributor. Thus, "the existence of one complaint about price in the files of the manufacturer could lead to a plausible inference that the complaint was the 'major cause' of the termination so as to make summary judgment [for the defendant] virtually impossible." See SENATE COMM. ON THE JUDICIARY, S. REP. NO. 42, 102d Cong., 1st Sess. at 26 (1991) [hereinafter SENATE REPORT] (on the Consumer Protection Against Price Fixing Act of 1991).

differences between horizontal and vertical conduct rather than on the formalistic distinction between price and nonprice restraints. A horizontal/vertical dichotomy for distributor terminations has been proposed by this author in earlier articles,¹¹ and the federal courts now seem to have laid the theoretical groundwork for accepting such an approach. The "ancillary restraints doctrine," first set forth by Judge (later Chief Justice) Taft in 1898, has recently been revitalized explicitly by a few lower federal courts and implicitly by the Supreme Court.¹² This doctrine provides a basis for substituting a horizontal/vertical dichotomy in distributor termination cases for the price/nonprice distinction. Indeed, in recent cases a few lower federal courts have expressly adopted a horizontal/vertical dichotomy for distributor terminations.¹³

Many courts and commentators have concluded that *Monsanto* and *Sharp* bar the approach to distributor terminations proposed in this article because the relevant inquiry under these decisions is not the source of a termination but its specific effect on competition in a relevant market.¹⁴ However, the source of a termination in itself reveals its competitive effect. The courts can thus use the horizontal/vertical dichotomy as a shorthand method of determining the market impact of a distributor termination. The Supreme Court has, in fact, recently recognized the utility of the horizontal/vertical dichotomy. In *Eastman Kodak Co. v. Image Technical Services Inc.*,¹⁵ the Supreme Court held that Kodak's refusal to deal with discounters who had been competing with it in the parts and service aftermarket could be deemed illegal on its face. The Court pointed out that, because the conduct at issue was horizontal rather than vertical, it could be found illegal without a full

11 See Thomas A. Piraino, Jr., *Sharp Dealing: The Horizontal/Vertical Dichotomy in Distributor Termination Cases*, 38 EMORY L.J. 311 (1989); Thomas A. Piraino, Jr., *Distributor Terminations Pursuant to Conspiracies Among a Supplier and Complaining Distributors: A Suggested Antitrust Analysis*, 67 CORNELL L. REV. 297 (1982).

12 See *United States v. Addyston Pipe and Steel Co.*, 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899). For a discussion of recent applications of the *Addyston Pipe* doctrine, see *infra* notes 183-91 and accompanying text.

13 See *ES Dev., Inc. v. RWM Enters., Inc.*, 939 F.2d 547 (8th Cir. 1991), *cert denied*, 112 S. Ct. 1176 (1992); *Lovett v. General Motors Corp.*, 769 F. Supp. 1506 (D. Minn. 1991); *Arnold-Pontiac GMC v. General Motors Corp.*, 700 F. Supp. 838 (W.D. Pa. 1988).

14 See *Bailey's Inc. v. Windsor America, Inc.*, 948 F.2d 1018 (6th Cir. 1991); *Ben Elfinan & Son, Inc. v. Criterion Mills, Inc.*, 774 F. Supp. 683 (D. Mass. 1991); *Toys "R" Us, Inc. v. R.H. Macy & Co.*, 728 F. Supp. 230 (S.D.N.Y. 1990); Michael Waldman & Jonathon W. Cuneo, *The Court is Winking at "Price Fixing,"* N.Y. TIMES, May 15, 1988, at F2.

15 112 S. Ct. 2042 (1992).

market analysis.¹⁶ *Eastman Kodak* represents a shift by the Court away from the manufacturer-oriented approach of *Monsanto* and *Sharp*. Under the rationale of *Eastman Kodak*, once a distributor proves that its termination was induced by a competitor, the termination should be deemed illegal without any further inquiry.¹⁷

Additional support for the horizontal/vertical dichotomy proposed in this Article can be found in several other cases decided by the Supreme Court during the last fifteen years. These cases can be viewed as establishing a new form of antitrust analysis as an intermediate standard between the traditional "per se" and "rule of reason" approaches. Under this new standard, the courts could inquire into whether a distributor termination was horizontally or vertically motivated. Once they had determined the parties' intent, they would not have to engage in an inquiry into the specific competitive effects of the termination.¹⁸ By referring to such precedent, the courts could fashion a new approach to distributor terminations that is neither as harsh to manufacturers as the proposed federal legislation nor as difficult for terminated distributors as the popular judicial interpretations of *Monsanto* and *Sharp*.

II. THEORETICAL DEFICIENCIES IN THE CURRENT JUDICIAL APPROACH

A. *The Per Se/Rule of Reason Conundrum*

The analysis of mixed termination cases has suffered from the courts' inability to choose a consistent theoretical basis for evaluating defendants' conduct. Traditionally, the federal courts have been preoccupied with whether a "per se" or "rule of reason" analysis should apply in such cases. Indeed, the outcome of mixed termination cases has usually depended upon the form of analysis chosen by a court. To date, most courts have regarded the per se rule and the rule of reason as opposite approaches to antitrust analysis. Under the per se rule, a defendant is conclusively presumed to have committed an antitrust violation when it engages in certain types of prohibited conduct. Once the conduct is proven, the defendant cannot escape liability by arguing that it had a procompetitive purpose or that the conduct had a beneficial effect.¹⁹ In contrast, under the rule of reason, the presumptions

16 *Id.* at 2084 n.18.

17 See *infra* notes 205-11 and accompanying text.

18 See *infra* notes 226-35 and accompanying text.

19 See, e.g., *FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411 (1990) (hor-

are in favor of the defendant. A plaintiff must prove a specific adverse effect on competition in a relevant market in order to prevail. The courts have felt compelled in rule of reason cases to consider every factor that might conceivably bear on the competitive purpose or effect of the restriction in question, including the defendant's share of the relevant product and geographic markets.²⁰ The requirement that plaintiffs prove a defendant's market power has been particularly burdensome.²¹ In fact, plaintiffs have so rarely prevailed in rule of reason cases that the approach has been equated with a rule of per se legality.²²

The traditional per se and rule of reason approaches thus inevitably result in opposite outcomes in antitrust cases. Courts applying the per se rule to mixed terminations have found them to be illegal on their face.²³ Under the rule of reason, however, terminated distributors have been unable to prove the requisite

izontal price-fixing); *United States v. Topco Assocs., Inc.*, 405 U.S. 596 (1972) (horizontal allocation of customers and territories).

20 In *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977), the Court stated that, "[u]nder this rule, the factfinder weighs all the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition." *Id.* at 49 (citing *Chicago Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918)). The *Sharp* Court cited *Sylvania's* broad definition of the rule of reason. *Sharp*, 485 U.S. at 723; see also Robert Pitofsky, *In Defense of Discounters: The No-Frills Case for a Per Se Rule Against Vertical Price-Fixing*, 71 GEO. L.J. 1487, 1489 (1983) (referring to "rule of reason" approach in which all relevant competitive factors are taken into account").

21 Professor Areeda has observed that proof of market power is "difficult, complex, expensive and time-consuming." Phillip Areeda, *The Changing Contours of the Per Se Rule*, 54 ANTITRUST L.J. 27, 28 (1985). A current Commissioner of the Federal Trade Commission has described the "exhaustive and exhausting document production by the . . . parties both in and close to the market, endless debates about elasticity of supply and demand, and all the minutiae that may need to be tied down in a full rule of reason case." Mary L. Azcuenaga, *Market Power as a Screen in Evaluating Horizontal Restraints*, 60 ANTITRUST L.J. 935, 940 (1992). Indeed, the Commissioner concluded that, when a market power inquiry is required under the rule of reason, most "cases would not be brought simply because the litigation cost would outweigh the benefits of the case" *Id.* at 936.

22 See William F. Baxter, *The Viability of Vertical Restraints Doctrine*, 75 CAL. L. REV. 933, 949 (1987) ("[A]s a practical matter, current case law treats all [nonprice] . . . vertical restraints as lawful per se [under the rule of reason]."). In fact, only two cases decided in the last fifteen years have found vertical restrictions to be illegal under the rule of reason. See *Graphic Prods. Distribs. v. Itek Corp.*, 717 F.2d 1560 (11th Cir. 1983) (airtight territorial restriction imposed by supplier which also operated at resale level); *Eiberger v. Sony Corp. of America*, 622 F.2d 1068 (2d Cir. 1980) (warranty "pass-over" fee involving competing distributors).

23 See *Zidell Explorations, Inc. v. Conval Int'l*, 719 F.2d 1465 (9th Cir. 1983); *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164 (3d Cir. 1979); *Lovett v. General Motors Corp.*, 769 F. Supp. 1506 (D. Minn. 1991).

injury to competition, and their claims have been dismissed on summary judgment.²⁴

B. The Price/NonPrice Dichotomy

Most courts have adopted the price/nonprice dichotomy as the basis for making the critical distinction between per se and rule of reason conduct. Unfortunately, this approach is based more on judicial tradition than on the actual economic purpose or effect of mixed terminations.

The price/nonprice dichotomy stems from the Supreme Court's 1977 decision in *Continental T.V., Inc. v. GTE Sylvania Inc.*²⁵ *Sylvania* is widely viewed as the Supreme Court's seminal recognition of the need to base antitrust rules on economic effect rather than on social goals such as the independence of small business.²⁶ In *Sylvania*, however, the Court stopped short of viewing the substantive economic purpose and impact of all conduct as determinative. *Sylvania* created a fundamental dichotomy between price and nonprice vertical restraints. The Court recognized that the rule of reason should apply to nonprice vertical restrictions because of their potential beneficial effect on competition. However, the Court was unwilling to overrule its long-established rule on the per se illegality of resale price maintenance.²⁷ Thus, future choices between per se and rule of reason analysis would have to be made on the basis of whether a supplier was enforcing a price or nonprice vertical restraint. This distinction would be difficult to make in subsequent cases because a manufacturer often has identical procompetitive purposes for these two types of vertical restraints.

24 See *The Jeanery, Inc. v. James Jeans, Inc.*, 849 F.2d 1148 (9th Cir. 1988); *Garment District, Inc. v. Belk Stores Servs., Inc.*, 799 F.2d 905 (4th Cir. 1986), cert. denied, 486 U.S. 1005 (1988); *McCabe's Furniture, Inc. v. La-Z-Boy Chair Co.*, 798 F.2d 323 (8th Cir. 1986), cert. denied, 486 U.S. 1005 (1988).

25 433 U.S. 36 (1977).

26 See Edward Brunet & David J. Sweeney, *Integrating Antitrust Procedure and Substance After Northwest Wholesale Stationers: Evolving Antitrust Approaches to Pleadings, Burden of Proof, and Boycotts*, 72 VA. L. REV. 1015, 1017 (1986).

27 *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 51 n.18 (1977). The rule was first established in 1911 in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911), and was subsequently reaffirmed on several occasions. See *Perma Life Mufflers, Inc. v. International Parts Corp.*, 392 U.S. 134 (1968); *Simpson v. Union Oil Co.*, 377 U.S. 13 (1964); *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960); *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707 (1944); *FTC v. Beech-Nut Packing Co.*, 257 U.S. 441 (1922).

At issue in *Sylvania* was a contractual requirement that distributors sell Sylvania television sets only from authorized locations. Although this requirement limited competition among the distributors in the resale of Sylvania televisions ("intra-brand competition"), the Court recognized that the restrictions also allowed Sylvania to achieve certain efficiencies in competing against other television manufacturers ("inter-brand competition").²⁸ The territorial protection afforded by the location clauses could, for example, induce distributors to make the investments necessary to provide more services to customers, thereby making the Sylvania brand more attractive to consumers. The Court noted that "because of market imperfections such as the so-called 'free-rider' effect," such services might not be provided by retailers in the absence of vertical restrictions.²⁹ In implementing such restrictions a supplier was likely to be exercising its best judgment on how to compete most effectively against other brands.³⁰ Emphasizing that such inter-brand competition "is the primary concern of antitrust law," the Court concluded that a rule of per se illegality was not appropriate for nonprice vertical restrictions such as Sylvania's location clause.³¹ Departure from the rule of reason standard, the Court pointed out, "must be based upon demonstrable economic effect rather than . . . upon formalistic line drawing."³² In analyzing nonprice vertical restrictions, a court should use the rule of reason to balance any restriction of intra-brand competition against the beneficial impact on inter-brand competition.³³

28 *Sylvania*, 433 U.S. at 51-57.

29 *Id.* at 55. The "free-rider" effect occurs when certain retailers providing high-cost presale services to customers (such as product demonstrations and advice) compete with other retailers who can charge a lower price because they do not provide such services. See F.M. Scherer, *The Economics of Vertical Restraints*, 52 ANTITRUST L.J. 687, 694 (1983). The low-cost retailer "free-rides" on the services provided by the other retailers. Frequently customers will obtain necessary product information and advice from the high-cost retailer and then purchase the product from the "free-rider" at a lower price. If enough customers are diverted by the free-rider, the high-cost retailers may ultimately be forced to cease providing customer services in order to remain competitive in the intra-brand market. See Lester G. Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86 (1960); Dennis O. Doherty, Note, *Business Electronics Corp. v. Sharp Electronics Corp.: Monsanto's Progeny and the Congressional Proposal to Codify the Per Se Rule Against Vertical Price Fixing*, 38 CATH. U. L. REV. 963, 992 (1989).

30 *Sylvania*, 433 U.S. at 54-56. Indeed, the Court concluded that, because manufacturers had a natural interest in insuring a low-cost, high-volume distribution policy, they would not be likely to limit intra-brand competition any more than was necessary to stimulate inter-brand competition. *Id.* at 56.

31 *Id.* at 52 n.19, 56-59.

32 *Id.* at 59.

33 *Id.* at 54-57. By this holding, the Court overruled its 1967 decision in *United*

The *Sylvania* Court did not extend this rule of reason approach to resale price restrictions. In a footnote, the Court stated that the per se rule should continue to apply to vertical price-related restraints because they "involve significantly different questions of analysis and policy."³⁴ However, as Justice White recognized in his concurring opinion, "the economic arguments in favor of allowing vertical non-price restraints generally apply to vertical price restrictions as well."³⁵ Resale price restrictions can be just as effective as nonprice restrictions in insuring customer services. Both types of restrictions can be designed to afford distributors a sufficient resale margin to afford such services.³⁶ Indeed, resale price restraints are a less stringent means of encouraging customer services. Vertical territorial restraints can preclude all competition between distributors in the resale of the supplier's products, but resale price restraints allow distributors to continue to compete in other areas, such as the delivery of customer services.³⁷

The price/nonprice dichotomy adopted in *Sylvania* is particularly difficult to make in mixed termination cases. Under *Sylvania*, the rule of reason would apply when a supplier terminated a distributor to enforce a nonprice vertical restraint, but the per se rule would apply if the termination was for a price-related reason.

States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967), which had applied the per se rule to nonprice vertical restraints.

34 *Sylvania*, 433 U.S. at 51 n.18. The Court noted that, unlike nonprice restraints, resale price restrictions might facilitate cartelizing. Cartels, however, are subject to direct per se attack as unjustified horizontal restrictions on competition. See *supra* note 19 and accompanying text. A per se rule against resale price restraints is therefore not necessary to prevent cartelization. The more likely rationale for the Court's continuation of the per se rule was the second reason cited in *Sylvania*: "Congress['] . . . approval of a per se analysis of vertical price restrictions." *Id.* For a discussion of the history of congressional support for a per se approach, see *infra* note 38 and accompanying text.

35 *Sylvania*, 433 U.S. at 69-70 (White, J., concurring).

36 Several commentators have pointed out the economic equivalence of price and nonprice vertical restraints. See, e.g., ROBERT H. BORK, *THE ANTITRUST PARADOX* 289 (1978); Wesley J. Liebler, *Resale Price Maintenance and Consumer Welfare*: Business Electronics Corp. v. Sharp Electronics Corp., 36 UCLA L. REV. 889, 893 (1989).

37 "The territorial restriction affects both price and service competition; the price restriction affects only price competition." Richard A. Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6, 9 (1981). See also Panel Discussion, *Antitrust Do's and Don'ts of Distribution*, 53 ANTITRUST L.J. 363, 377-78 (1984) (comments of Harry M. Reasoner). In *Eastern Scientific Co. v. Wild Heerbrugg Instruments*, 572 F.2d 883 (1st Cir.), cert. denied, 439 U.S. 833 (1978), the First Circuit held that a manufacturer could control a dealer's resale prices on sales outside of the dealer's territory because the impact on competition would be less than if the manufacturer had imposed an airtight territorial restriction forbidding such sales entirely.

The distinction between "price" and "nonprice" reasons for a termination, however, is illusory. A manufacturer may be concerned about a dealer's narrow resale margins because they prevent the dealer from providing customer services. Thus, a dealer may complain to a manufacturer about another dealer's price-cutting, and the manufacturer may legitimately respond by terminating the dealer for a "nonprice" reason such as the failure to provide adequate assistance to consumers.

In *Monsanto* and *Sharp* the Supreme Court was rightfully concerned about a court's ability to distinguish legitimate "nonprice" motives from illegal "price-related" motives in mixed termination cases. An obvious solution to this problem simply would have been to overrule the per se illegality of resale price restrictions and apply an identical rule of reason analysis to all vertical restraints. However, the *Monsanto* and *Sharp* Courts were no more capable of overruling the per se illegality of resale price maintenance than was the *Sylvania* Court. Prompted either by stare decisis or by clear congressional opposition to a change in analysis,³⁸ the Court in both cases reaffirmed the per se approach.³⁹

With a clear distinction between price and nonprice vertical restraints so firmly established, the Court faced a difficult dilemma: how to protect *Sylvania's* recognition of the potential beneficial effects of nonprice vertical restraints when nearly indistinguishable price-related restraints were per se illegal. The Court's solution in *Monsanto* and *Sharp* was to restrict the circumstances in which the per se rule could be invoked. In its zeal to protect the

38 Congressional actions since the mid-1970s have demonstrated consistent support for the per se rule against resale price maintenance. In 1975, Congress repealed the so-called "fair trade" exemption for certain state-authorized resale price maintenance agreements. Consumer Goods Pricing Act of 1975, 15 U.S.C. §§ 1, 45 (1988). When Congress repealed the fair trade laws, it "fully understood that it was adopting the per se rule prohibiting vertical price-fixing." John F. Seiberling, *Congress Makes Laws: The Executive Should Enforce Them*, 53 ANTITRUST L.J. 175, 177 (1984). Appropriations bills for the Department of Justice during the 1980s consistently prohibited the use of funds for altering the per se rule against resale price maintenance. See *White House Opposes Authorization of Justice Department with RPM Rider*, 52 Antitrust & Trade Reg. Rep. (BNA) No. 1320, at 1127 (June 18, 1987). A 1985 House of Representatives resolution criticized the Vertical Restraints Guidelines of the Department of Justice for "qualifying the accepted rule that vertical price-fixing in any context is illegal per se." H.R.J. Res. 303, 99th Cong., 1st Sess., 131 Cong. Rec. H9324 (daily ed. Oct. 29, 1985). The versions of the Price Fixing Prevention Act passed by the House and Senate in the 102d Congress codify the per se rule against resale price-fixing. See 60 Antitrust & Trade Reg. Rep. (BNA) No. 1515, at 652 (May 9, 1991); 60 Antitrust & Trade Reg. Rep. (BNA) No. 1521, at 847 (June 20, 1991).

39 *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 761 (1984); *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 724 (1988).

Sylvania doctrine, the Court adopted formalistic grounds for distinguishing between per se and rule of reason conduct. Indeed, the approach taken by the Court in *Monsanto* and *Sharp* violated its own admonition in *Sylvania* that antitrust analysis be based on "demonstrable economic effect."⁴⁰ In *Monsanto* the Court concluded that a manufacturer's termination of a price-cutting distributor "in response to" complaints from higher priced dealers was insufficient to raise the inference of a resale price-fixing conspiracy.⁴¹ In *Sharp* the Court termed the induced termination of a discounter a "nonprice vertical restraint" subject to rule of reason analysis.⁴² A per se illegal conspiracy could only be found, the Court concluded, in those rare cases in which the supplier and remaining distributor agreed on the specific resale price to be charged after a discounter's termination.⁴³

Precluded by *Monsanto* and *Sharp* from proceeding under a per se theory, terminated distributors' only alternative in the lower federal courts has been the rule of reason. Plaintiffs have had little chance of prevailing under traditional rule of reason theories, which require proof of specific adverse market effects.⁴⁴ Indeed, following *Sharp*, most lower federal courts have dismissed terminated distributors' claims even in the face of substantial evidence that the terminations were induced by a competitor.⁴⁵

III. MIXED TERMINATION LAW PRIOR TO *MONSANTO*

The federal courts' approach to mixed termination cases has not always been so formalistic. In a series of cases prior to the *Monsanto* decision in 1984, the Supreme Court and lower federal courts concentrated on the legitimate economic difference between horizontal and vertical conduct rather than on the formalistic distinction between price and nonprice restraints.

40 *Sylvania*, 433 U.S. at 59.

41 *Monsanto*, 465 U.S. at 763.

42 *Sharp*, 485 U.S. at 727.

43 *Id.*

44 Terminated distributors find it nearly impossible to prevail under the rule of reason because they cannot show a specific adverse competitive effect in the interbrand market. After the termination of a distributor, total sales of the relevant brand may be unaffected, and prices in the interbrand market may not immediately increase. Thus, no general "injury to competition" occurs in the interbrand market because "neither aggregate output nor prices have changed." Harry S. Gerla, *Discounters and the Antitrust Laws: Faces Sometimes Should Make Cases*, 12 J. CORP. L. 1, 11-12 (1986).

45 See *infra* cases cited in notes 86-87, 113-14.

In *Klor's, Inc. v. Broadway-Hale Stores Inc.*,⁴⁶ a retailer induced certain appliance manufacturers and distributors to sell to a competing retailer (Klor's) only at discriminatorily high prices. The Court pointed out that the inducing retailer had initiated a "group boycott" by enlisting the support of firms at a different competitive level to take the adverse action against Klor's. The Court applied the per se rule despite the seemingly vertical form of the conspiracy. It was sufficient for illegality that Klor's had been driven out of the appliance distribution business as a result of the actions of one of its competitors.⁴⁷

In *United States v. General Motors Corp.*,⁴⁸ the group boycott was organized by several Chevrolet dealers who induced General Motors to prohibit its dealers from selling automobiles to discounters. The Court recognized that the vertical form of the conspiracy should not insulate the defendants from per se liability.⁴⁹ Indeed, the Court pointed out that, by convincing General Motors to participate in the arrangement, the Chevrolet dealers had made their conspiracy to exclude discounters from the market even more effective than it otherwise would have been.⁵⁰

*United States v. Topco Associates, Inc.*⁵¹ involved agreements among a group of grocery stores not to sell the Topco private

46 359 U.S. 207 (1959).

47 *Id.* at 212-13.

48 384 U.S. 127 (1966).

49 One court has explained that the Supreme Court's application of the per se rule in *General Motors* "points to the importance of the underlying horizontal nature of the arrangement Substance should be more important than form." *Battle v. Lubrizol Corp.*, 673 F.2d 984, 989 (8th Cir. 1982), *aff'd sub nom. Battle v. Watson*, 712 F.2d 1238 (8th Cir. 1983) (en banc), *cert. denied*, 466 U.S. 931 (1984); *see also* *ES Dev., Inc. v. RWM Enters., Inc.*, 939 F.2d 547, 557 (8th Cir. 1991) ("[A]lthough *General Motors'* action on its face seemingly imposed a vertical restraint in response to vertical activity from individual dealers, it came as a result of inducements emanating from a horizontal agreement among the dealers to constrain competitive activity at the same dealer level."), *cert. denied*, 112 S. Ct. 1176 (1992).

50 *General Motors*, 384 U.S. at 144. Inducement of aid from a higher competitive level has been recognized as the defining characteristic of a group boycott. *See* Richard M. Buxbaum, *Boycotts and Restrictive Marketing Arrangements*, 64 MICH. L. REV. 671 (1966):

[A]n economic boycott requires the cooperation of a party at a different level in the distribution process from that on which the instigators operate. Even though members of an industry wish to punish or eliminate a certain competitor, they can do so only by inducing the competitor's customers or suppliers to stop dealing with him.

Id. at 674-75; *see also* LAWRENCE A. SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST § 148 (1977).

51 405 U.S. 596 (1972).

label brand in each other's territories. The defendants had formed a single entity to act as their purchasing agent and to license each store to sell the Topco brand. Despite the apparent vertical form of the arrangement, the Court looked to the competitive substance of the defendants' conduct and termed it a per se illegal horizontal allocation of territories.⁵²

Sylvania, which was decided after each of these cases, did not limit the per se analysis of *Klor's*, *General Motors*, and *Topco*. The Court made clear in *Sylvania* that its new rule of reason approach for nonprice vertical restrictions should not apply to horizontally induced restraints. The Court specifically cited *General Motors* and *Topco* with approval and confirmed that "there is no doubt that" the per se rule should continue to apply to "horizontal restrictions originating in agreements among . . . retailers."⁵³ Thus, in addition to creating the price/nonprice dichotomy, the *Sylvania* Court also reaffirmed the more rational economic distinction between horizontal and vertical conduct.

In the years immediately after the *Sylvania* decision, the lower federal courts had several occasions in which to consider the distinction between horizontal and vertical conduct in mixed termination cases. Retail discounting became more prevalent as inflation grew in the late 1970s. Consumers began to search out low-price dealers as a means of minimizing inflationary price increases. In an attempt to protect their customer base, full-price retailers complained more frequently to suppliers about cost cutting by their competitors.⁵⁴ In a series of cases the lower federal courts focused on the antitrust implications of terminations of price-cutting distributors allegedly induced by such complaints. Several courts held that these terminations were per se illegal because they had horizontal effects, even though they were the product of what could be characterized as a vertical agreement.

In many of these cases, only one distributor was the alleged instigator of a competitor's termination. Thus the form of the agreement was entirely vertical (that is, between the supplier and a single instigating dealer). Nevertheless, several courts concluded that such terminations should be per se illegal because they eliminated competition at the resale level for no beneficial purpose. In

52 *Id.* at 608, 610-11.

53 *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 58 n.28 (1977).

54 See William G. Southlard, *Monsanto Co. v. Spray-Rite Service Corp.: Providing Upstream and Downstream Concerted Action*, 10 DEL. J. CORP. L. 673, 681-82 (1985).

Cernuto, Inc. v. United Cabinet Corp.,⁵⁵ for example, a retailer of kitchen cabinets convinced a cabinet manufacturer to terminate a competing retailer who was discounting the cabinets. Instead of classifying the termination as vertical and applying a *Sylvania* rule of reason analysis, the court recognized that the horizontal competitive effect of the termination mandated a per se approach:

When a manufacturer acts on its own, in pursuing its own market strategy, it is seeking to compete with other manufacturers by imposing what may be defended as reasonable vertical restraints. This would appear to be the rationale of the *GTE Sylvania* decision. However, if the action of a manufacturer or other supplier is taken at the direction of its customer, the restraint becomes primarily horizontal in nature in that one customer is seeking to suppress its competition by utilizing the power of a common supplier. Therefore, although the termination in such a situation is, itself, a vertical restraint, the desired impact is horizontal and on the dealer, not the manufacturer, level . . . It is just this type of conduct that the antitrust laws were designed to reach.⁵⁶

Many federal courts subsequently adopted the *Cernuto* approach and applied the per se rule when a single distributor induced a supplier to terminate a competing distributor.⁵⁷ Several other courts indicated in dicta that they would follow the *Cernuto* rule.⁵⁸

⁵⁵ 595 F.2d 164 (3d Cir. 1979).

⁵⁶ *Id.* at 168-69.

⁵⁷ See *Zidell Explorations Inc. v. Conval Int'l*, 719 F.2d 1465 (9th Cir. 1983) (valve distributor induced foreign manufacturer to terminate competitor); *Alloy Intern. Co. v. Hoover-NSK Bearing Co.*, 635 F.2d 1222 (7th Cir. 1980) (bearing distributor terminated at request of competitor); *Sport Shoe of Newark, Inc. v. Ralph Libonati Co., Inc.*, 512 F. Supp. 921 (D. Del. 1981) (shoe retailer induced supplier not to sell to new retailer at nearby location). The *Cernuto* approach was anticipated as early as 1963 in *Girardi v. Gates Rubber Co.*, 325 F.2d 196 (9th Cir. 1963), where the court found a belt manufacturer per se liable for conspiring with a distributor to terminate one of its price-cutting competitors.

In *Cernuto* and many of its progeny the terminated distributor was a price-cutter. Thus, in addition to the anticompetitive horizontal aspects of the termination, the courts were able to use resale price maintenance as a rationale for applying the per se rule. See, e.g., *Cernuto*, 595 F.2d at 170; *Zidell Explorations*, 719 F.2d at 1469-70. However, some courts expressly recognized that the per se rule is appropriate whenever one or more distributors induce a supplier to terminate a rival, regardless of whether the maintenance of resale prices is a specific object of the conspiracy. See, e.g., *Sport Shoe*, 512 F. Supp. at 924 (termination of potential competitor at behest of distributor per se illegal even in absence of price-related motive).

⁵⁸ See *Roesch, Inc. v. Star Cooler Corp.*, 712 F.2d 1235, 1237 (8th Cir. 1983) (en banc), *cert. denied*, 466 U.S. 926 (1984); *JBL Enters., Inc. v. Jhirmack Enters., Inc.*, 698

The *Cernuto* approach was not, however, unanimously followed in the federal courts. Some circuit courts found it impossible to disregard the outward vertical form of a termination induced by a single competitor. In *Oreck Corp. v. Whirlpool Co.*,⁵⁹ for example, Sears Roebuck Co., the plaintiff's principal competitor in the resale of vacuum cleaners, had convinced Whirlpool to stop selling vacuum cleaners to the plaintiff. The court held that the per se rule could not apply because there was no horizontal plurality, that is, two or more defendants on the same distribution level.⁶⁰ Several other circuit courts have adopted an approach similar to *Oreck* and denied application of the per se rule when only one distributor allegedly induced a rival's termination.⁶¹

Such an approach to mixed terminations is arbitrary. For a finding of illegality, it should suffice that a termination was motivated by the anticompetitive demands of one or more competing distributors rather than by the procompetitive interbrand concerns of the supplier. The competitive evil in mixed termination cases results from the naked restriction of intrabrand competition effected by the conspiracy, not from the number of distributors on the inducing level.

IV. THE EFFECT OF *MONSANTO* AND *SHARP* ON MIXED TERMINATION LAW

Monsanto and *Sharp* represented a retreat from the substantive approach under which many federal courts had been analyzing distributor termination cases. In *Monsanto* and *Sharp* the Supreme Court reverted to a formalistic analysis of mixed terminations. This reversion was caused by the Court's dissatisfaction with the per se rule against resale price maintenance. Unable to directly overrule the per se approach, the Court nevertheless attempted to limit the circumstances in which the rule would apply. In *Monsanto* the Court did so by reinvigorating a formalistic distinction between

F.2d 1011, 1015 (9th Cir. 1983); *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 743 (7th Cir. 1982); *Battle v. Lubrizol Corp.*, 673 F.2d 984, 988-90 (8th Cir. 1982), *aff'd sub nom. Battle v. Watson*, 712 F.2d 1238 (8th Cir. 1983) (en banc), *cert. denied*, 466 U.S. 931 (1984); *Com-Tel, Inc. v. DuKane Corp.*, 669 F.2d 405, 409 (6th Cir. 1982); *Contractor Util. Sales v. Certain-Teed Prods.*, 638 F.2d 1061, 1072 (7th Cir. 1981).

59 579 F.2d 126 (2d Cir.) (en banc), *cert. denied*, 439 U.S. 946 (1978).

60 *Id.* at 131-32.

61 See, e.g., *Westman Comm'n Co. v. Hobart Int'l Inc.*, 796 F.2d 1216 (10th Cir. 1986); *Packard Motor Car Co. v. Webster Motor Car Co.*, 243 F.2d 418 (D.C. Cir.), *cert. denied*, 355 U.S. 822 (1957).

unilateral and concerted conduct which had been established early in the century.

Liability under section 1 of the Sherman Act is predicated on the existence of a "contract, combination . . . or conspiracy, in restraint of trade."⁶² Thus, a unilaterally adopted distribution policy does not violate section 1. The Supreme Court recognized as early as 1919 that a manufacturer could not be liable for resale price maintenance when it acted on its own to implement a particular distribution policy. In *United States v. Colgate Co.*,⁶³ the Court held that a manufacturer had the right to announce its suggested resale prices in advance and unilaterally refuse to deal with any customers who would not agree to observe the prices.

In the sixty-five years between the *Colgate* and *Monsanto* decisions, the Court progressively narrowed the *Colgate* doctrine. Any action taken by a supplier, beyond a simple refusal to deal, to insure or enforce adherence to its resale prices was deemed sufficient to infer a per se illegal resale price-fixing conspiracy.⁶⁴ In many cases the action consisted of a form of coercion aimed at forcing an unwilling buyer to comply with the manufacturer's suggested resale prices.⁶⁵ By the time of *Monsanto*, "relatively little . . . [was] left of the [*Colgate*] doctrine."⁶⁶

The *Monsanto* Court revitalized the *Colgate* doctrine. Spray-Rite, a distributor of Monsanto products, had alleged that competing distributors' complaints about Spray-Rite's failure to comply with Monsanto's suggested resale prices had caused Monsanto to effect its termination.⁶⁷ The Seventh Circuit had held that proof of termination "in response to" the complaints was sufficient to infer a

62 15 U.S.C. § 1 (1988).

63 250 U.S. 300 (1919).

64 See *Albrecht v. Herald Co.*, 390 U.S. 145 (1968) (attempts to solicit customers of noncomplying party); *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960) (threats to withhold deliveries); *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707 (1944) (enlisting assistance of wholesalers in assuring retailers' compliance); *FTC v. Beech-Nut Packing Co.*, 257 U.S. 441 (1922) (enforcement through special agents, blacklists, and refusals to deal); *United States v. A. Schrader's Son, Inc.*, 252 U.S. 85 (1920) (efforts to enforce resale prices through licensing contracts).

65 See *Parke, Davis & Co.*, 362 U.S. at 45-47; *Bausch & Lomb Optical Co.*, 321 U.S. at 723; *A. Schrader's Son*, 252 U.S. at 95, 99-100; *Beech-Nut Packing Co.*, 257 U.S. at 454-55; *Black Gold, Ltd. v. Rockwool Indus.*, 729 F.2d 676, 686 (10th Cir.) (threats of termination), *cert. denied*, 430 U.S. 946 (1984); *Yentsch v. Texaco, Inc.*, 630 F.2d 46, 54-55 (2d Cir. 1980) (threats of termination).

66 *Posner, supra* note 37, at 23 n.62; see also Donald F. Turner, *The Definition of Agreement Under the Sherman Act: Conscious Parallelism and Refusals to Deal*, 75 HARV. L. REV. 655, 685 (1962).

67 *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 756-59 (1984).

resale price-fixing conspiracy.⁶⁸ The Supreme Court emphasized that "distributors are an important source of information for manufacturers" and that "[a] manufacturer and its distributors have legitimate reasons to exchange information about . . . prices."⁶⁹ A manufacturer could be concerned about its distributors' resale margins for proper "nonprice" reasons, such as the need to assure that "distributors earn sufficient profit" to pay for various presale services.⁷⁰ Indeed, under *Colgate*, a manufacturer could unilaterally refuse to deal with distributors who failed to comply with its suggested resale prices. If an inference of conspiracy could be drawn from ambiguous evidence such as the receipt of price-cutting complaints, the beneficial exchange of resale pricing information would be deterred and a manufacturer's rights under *Colgate* would be unduly limited.⁷¹ Terminated distributors would therefore have to prove "something more" than a supplier's mere receipt of complaints:

Permitting an agreement to be inferred merely from the existence of complaints, or even from the fact that termination came about "in response to" complaints, could deter or penalize perfectly legitimate conduct. . . .

[S]omething more than evidence of complaints is needed. There must be evidence that tends to exclude the possibility that the manufacturer and nonterminated distributors were acting independently [T]he antitrust plaintiff should present direct or circumstantial evidence that reasonably tends to prove that the manufacturer and others "had a conscious commitment to a common scheme designed to achieve an

68 *Spray-Rite Serv. Corp. v. Monsanto Co.*, 684 F.2d 1226, 1239 (7th Cir. 1982). Prior to *Monsanto*, the circuit courts were divided over whether a manufacturer's mere receipt of complaints from other distributors about a terminated distributor's price-cutting was sufficient to support an inference of a per se illegal resale price-fixing conspiracy. For cases finding the receipt of complaints to be sufficient, see *Bostick Oil Co. v. Michelin Tire Corp.*, 702 F.2d 1207 (4th Cir.), *cert. denied*, 464 U.S. 894 (1983); *Battle v. Lubrizol Corp.*, 673 F.2d 984 (8th Cir. 1982), *aff'd sub nom. Battle v. Watson*, 712 F.2d 1238 (8th Cir. 1983) (en banc), *cert. denied*, 466 U.S. 931 (1984); *Girardi v. Gates Rubber Co.*, 325 F.2d 196 (9th Cir. 1963). For cases requiring evidence of something more, see *Bruce Drug, Inc. v. Hollister, Inc.*, 688 F.2d 853 (1st Cir. 1982); *Davis-Watkins Co. v. Service Merchandise*, 686 F.2d 1190 (6th Cir. 1982), *cert. denied*, 466 U.S. 931 (1984); *Schwimmer v. Sony Corp. of America*, 677 F.2d 946 (2d Cir.), *cert. denied*, 459 U.S. 1007 (1982); *Roesch, Inc. v. Star Cooler Corp.*, 671 F.2d 1168 (8th Cir. 1982), *aff'd*, 712 F.2d 1235 (8th Cir. 1983) (en banc), *cert. denied*, 466 U.S. 926 (1984); *Edward J. Sweeney & Sons, Inc. v. Texaco, Inc.*, 637 F.2d 105 (3d Cir. 1980), *cert. denied*, 451 U.S. 911 (1981).

69 *Monsanto*, 465 U.S. at 762.

70 *Id.* at 762-63.

71 *Id.* at 761, 763.

unlawful objective."⁷²

The Court pointed out that proof of such a conscious commitment would require evidence that a distributor had willingly participated in a supplier's resale price-fixing scheme. A plaintiff would have to show "both that the distributor communicated its acquiescence or agreement [to resale price-fixing], and that this was sought by the manufacturer."⁷³

In reaffirming *Colgate*, the *Monsanto* Court diverted attention from the substantive economic effect of defendants' activities to the formalistic distinction between unilateral and concerted conduct. The Court's concentration on the conspiracy issue implied that the simple existence of an agreement was enough to prove liability under section 1. The mutual agreement of a supplier and complaining distributor to effect another distributor's termination, however, does not prove that the termination had an anticompetitive effect. Indeed, the *Colgate* doctrine, as reborn in *Monsanto*, bears no relationship to the economic purpose or effect of defendants' conduct in mixed termination cases. Even the *Monsanto* Court conceded that the economic effect of unilateral and concerted action "is in many, but not all, cases similar or identical. . . . [J]udged from a distance, the conduct of the parties in the various situations can be indistinguishable."⁷⁴ There is no difference in economic effect between a distributor's willing compliance in a resale price maintenance program, which would be illegal under *Monsanto*, and its unwilling compliance, which *Monsanto* implied would be permissible. In fact, earlier cases had taken the view that *unwilling* compliance would have a more adverse economic effect.⁷⁵

72 *Id.* at 763-64 (quoting *Edward J. Sweeney & Sons*, 637 F.2d at 111.). *Sweeney*, like *Monsanto*, had involved a claim that a price-cutting distributor was terminated following the manufacturer's receipt of complaints from competitors. The court held that the mere receipt of complaints was not sufficient to infer the existence of a resale price-fixing conspiracy. *Edward J. Sweeney & Sons*, 637 F.2d at 111.

73 *Monsanto*, 465 U.S. at 764 n.9.

74 *Id.* at 762; see also HOUSE COMM. ON THE JUDICIARY, PRICE FIXING PREVENTION ACT OF 1991, H.R. REP. NO. 237, 102 Cong., 1st Sess. 16 (1991) [hereinafter HOUSE REPORT] ("The [*Monsanto*] Court would not have strained common usage or precedent if it had found instead that a manufacturer's refusal to deal with a distributor, or its threat of such action resulting in a distributor's compliance with announced policy, constituted concerted action.").

75 See cases cited *supra* note 64. By requiring "communicated acquiescence" in a resale price maintenance conspiracy, *Monsanto* appeared to change the rationale for inferring conspiracy (which had previously been based upon a manufacturer's coercion of a distributor's unwilling compliance) to a voluntary standard. There was no discernable eco-

The Court's requirement for a "conscious commitment to a common scheme"⁷⁶ was borrowed from horizontal antitrust cases, in which the requirement makes more sense.⁷⁷ Parties at the same distribution level are likely to share the same anticompetitive purpose for a restraint. In the vertical context, however, the parties have different competitive purposes for agreeing to a restraint on competition. The supplier's purpose for effecting a termination is to promote interbrand competition, while the distributors' purpose in inducing a termination is to limit competition among themselves.⁷⁸ The most important issue in a mixed termination case is thus not whether a supplier and complaining distributor each had a "conscious commitment" to a termination; it is usually obvious that they did. The decisive factor should be which party's purposes were intended to be served by the termination.

Monsanto provides no economic guideposts for the courts to use in determining the legality of a mixed termination, but only uncertain distinctions between independent and concerted actions.⁷⁹ In fact, the *Monsanto* Court never explained how it applied its new conspiracy standard to the facts of the case. Despite the Court's language establishing a high threshold for inferring a conspiracy, the Court affirmed a \$10.5 million judgment against Monsanto.⁸⁰ The facts emphasized by the Court were circumstantial and gave little, if any, indication of a meeting of the minds between Monsanto and the complaining distributors. The Court appeared to hold Monsanto liable on the basis of various actions taken against other distributors after the termination to enforce their adherence to resale prices.⁸¹ Observers have thus concluded

conomic reason for this change. Indeed, the Court's original distinction between coerced and willing compliance has been criticized for its lack of economic substance. As one commentator stated, "the effect on the market was the same in the *Colgate* unilateral action situation as in the case where the manufacturer took some additional steps and thereby became part of an agreement." Jean W. Burns, *Rethinking the "Agreement" Element in Vertical Antitrust Restraints*, 51 OHIO ST. L.J. 1, 19 (1990).

76 *Monsanto*, 465 U.S. at 764, 768.

77 See Burns, *supra* note 75, at 38-39.

78 See *infra* notes 129-37 and accompanying text.

79 *Monsanto*, 465 U.S. at 764.

80 *Id.* at 765-68.

81 *Id.* After the termination, Monsanto advised distributors that it would not continue to supply them with herbicide if they cut their resale prices. This fact was communicated to distributors during the critical spring shipping season when herbicide was in short supply. *Id.* at 765 n.10.

"that the Court's treatment of the facts in *Monsanto* was inconsistent with the tenor of its rhetoric."⁸²

It is not surprising, then, that the lower federal courts have found the *Monsanto* conspiracy standard confusing and difficult to apply. The lower courts' interpretation of *Monsanto* has been described as a "confusing welter of . . . semantic formulations."⁸³ Most federal courts have, however, agreed on one aspect of the *Monsanto* case: the high hurdle which plaintiffs must meet to survive summary disposition on the conspiracy issue.⁸⁴ This strict interpretation derives from the *Monsanto* Court's unfortunate statement that even a termination "in response to" complaints is insufficient to infer a conspiracy.⁸⁵ In many post-*Monsanto* cases there was substantial evidence that a termination was effected as a result of competing distributors' complaints, and yet the courts were willing to accept any plausible justification offered by a defendant to rebut the inference of conspiracy.⁸⁶ Indeed, in more than one-

82 Terry Calvani & Andrew G. Berg, *Resale Price Maintenance After Monsanto: A Doctrine Still at War With Itself*, 1984 DUKE L.J. 1163, 1197.

83 Mark E. Rozkowski, *The Sad Legacy of GTE Sylvania and its Rule of Reason: The Dealer Termination Cases and the Demise of Section 1 of the Sherman Act*, 22 CONN. L. REV. 129, 187 (1989); see also Sanford M. Litvack, *The Future Viability of the Current Antitrust Treatment of Vertical Restraints*, 75 CAL. L. REV. 955, 957 (1987). The Supreme Court itself has had difficulty characterizing the *Monsanto* test. In *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986), the Court appeared to interpret *Monsanto* to preclude an inference of conspiracy even when the evidence presented by the plaintiff and defendant was evenly balanced: "[C]onduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy." *Id.* at 588.

84 See, e.g., *Parkway Gallery Furniture, Inc. v. Kittinger/Pennsylvania House Group, Inc.*, 878 F.2d 801 (4th Cir. 1989) (summary judgment granted for manufacturer despite evidence that manufacturer sought pricing assurances from dealers); *H.C. Hayden Co. v. Siemens Medical Sys. Inc.*, 879 F.2d 1005 (2d Cir. 1989) (summary judgment for manufacturer not precluded by evidence of meetings between complaining dealers and manufacturer to discuss termination); *Terry's Floor Fashions, Inc. v. Burlington Indus., Inc.*, 763 F.2d 604 (4th Cir. 1985) (no inference of conspiracy allowed when manufacturer discussed termination with other dealers).

85 *Monsanto*, 465 U.S. at 764.

86 See, e.g., *The Jeanery, Inc. v. James Jeans, Inc.*, 849 F.2d 1148 (9th Cir. 1988) (termination consistent with independent action under *Colgate* despite fact that manufacturer received threats that distributors would cease doing business if manufacturer did not terminate plaintiff); *Garment Dist., Inc. v. Belk Stores Servs., Inc.*, 799 F.2d 905 (4th Cir. 1986) (verdict directed against plaintiff despite evidence of acquiescence to threats from competing retailer), *cert. denied*, 486 U.S. 1005 (1988); *McCabe's Furniture, Inc. v. La-Z-Boy Chair Co.*, 798 F.2d 323 (9th Cir. 1986) (evidence of termination of discounter to placate complaining dealer insufficient to raise inference of resale price-fixing conspiracy), *cert. denied*, 486 U.S. 1005 (1988). Thus, under the federal courts' interpretation of *Monsanto*, plaintiffs must "disprove the existence of any or all hypothetical explanations for the manufacturer's conduct that might justify a dealer termination." HOUSE REPORT,

half of the mixed termination cases decided since *Monsanto*, the courts have granted summary judgement or a directed verdict for the defendant.⁸⁷ Thus, in a very real sense, the language of the *Monsanto* decision has triumphed over its holding.⁸⁸

Unlike *Monsanto*, which concerned the procedural issue of conspiracy, *Sharp* dealt with the substantive question of the scope of the resale price-fixing offense in mixed termination cases. In *Sharp*, the Court once again adopted a formalistic basis for limiting the rights of terminated distributors. Because *Sharp* involved the substantive definition of an antitrust offense, its holding could have an even more adverse effect on plaintiffs than *Monsanto*.

The issue in *Sharp* was whether the per se rule should apply when a single distributor induced a supplier to terminate a price-cutting competitor. The *Cernuto* line of cases had applied a per se analysis in such instances, reasoning that an induced termination amounted to a naked restriction of intrabrand competition with no redeeming interbrand effect.⁸⁹ Other federal courts, however, had held that, even when a competing distributor induced the termination of a price cutter, the per se rule should not apply unless the manufacturer and remaining dealer agreed on a specific resale price to be charged in the future.⁹⁰

It was clear in *Sharp* that the plaintiff's termination had been induced by a competitor. Business Electronics Corporation ("Busi-

supra note 74, at 13.

87 Kyle M. N. Jones, Comment, *Resale Price Maintenance and the Evidentiary Standard for Sherman Act Conspiracy: When Is Enough Enough?*, 66 U. DET. L. REV. 713, 729 (1989).

88 See HOUSE REPORT, *supra* note 74, at 23. Some lower federal courts, however, have considered the facts of *Monsanto* to be more important than its rhetoric and have been willing to infer a conspiracy from circumstantial evidence. See, e.g., *Big Apple BMW, Inc. v. BMW of N. Am., Inc.*, 1992-2 Trade Cas. (CCH) ¶ 69,918 (3d Cir. 1992); *Helicopter Support Sys., Inc. v. Hughes Helicopter, Inc.*, 818 F.2d 1530 (11th Cir. 1987); *Arnold Pontiac-GMC, Inc. v. General Motors Corp.*, 786 F.2d 564 (3d Cir. 1986); *Tunis Bros. Co. v. Ford Motor Co.*, 763 F.2d 1482 (3d Cir. 1985), *vacated*, 475 U.S. 105 (1986), *and cert. denied*, 112 S. Ct. 3034 (1992); *Lovett v. General Motors Corp.*, 769 F. Supp. 1506 (D. Minn. 1991).

89 See *supra* notes 55-58 and accompanying text. As the court stated in *World of Sleep, Inc. v. La-Z-Boy Chair Co.*, 756 F.2d 1467 (10th Cir. 1985), *cert. denied*, 474 U.S. 823 (1985), "The relevant consideration is not whether a specific price is set, but whether a dealer's independent judgment is eliminated through a coerced agreement." *Id.* at 1477.

90 See *Morrison v. Murray Biscuit Co.*, 797 F.2d 1430, 1440 (7th Cir. 1986); *Westman Comm'n Co. v. Hobart Int'l, Inc.*, 796 F.2d 1216, 1223-24 (10th Cir. 1986), *cert. denied*, 486 U.S. 1005 (1988); *National Marine Elec. Distrib., Inc. v. Raytheon Co.*, 778 F.2d 190, 193 (4th Cir. 1985); *JBL Enters., Inc. v. Jhirmack Enters., Inc.*, 698 F.2d 1011, 1015 (9th Cir.), *cert. denied*, 464 U.S. 829 (1983).

ness Electronics"), a Houston dealer for Sharp Electronics Corp. ("Sharp"), competed with Gilbert Hartwell, the only other Sharp distributor in Houston. Business Electronics' retail prices were lower than Hartwell's. Hartwell complained to Sharp on several occasions about Business Electronics' lower prices. Hartwell finally gave Sharp an ultimatum: unless Sharp terminated Business Electronics within thirty days, Hartwell would cease doing business with Sharp. Sharp responded to Hartwell's threat by terminating Business Electronics within the thirty-day period.⁹¹ The jury concluded that Sharp and Hartwell had entered into an agreement to terminate Business Electronics because of its price-cutting.⁹²

The Supreme Court held that the per se rule was inapplicable because Sharp and Hartwell had not agreed on the specific prices to be charged by Hartwell after Business Electronics' termination.⁹³ As in *Monsanto*, the Court feared an overly broad application of the per se rule against resale price maintenance. The Court pointed out that, under a per se approach, a manufacturer's termination of a price-cutter would be unduly risky. The manufacturer would find it difficult to prove that its real motivation for the termination was to insure adequate customer services rather than to protect a dealer's profit margin.⁹⁴ Reaffirming *Sylvania's* determination that "interbrand competition is the primary concern of the antitrust laws,"⁹⁵ the Court concluded that "a rule of *per se* illegality . . . was not needed or effective to protect intrabrand competition."⁹⁶ The Court stated that the purpose of the per se rule against resale price maintenance was to prevent *interbrand* cartels.⁹⁷ Vertical price agreements could facilitate such cartels by "reducing the manufacturer's incentive to cheat . . . since its retailers could not pass on lower prices to consumers."⁹⁸ Retailers, however, would only be prevented from passing along lower prices when they had agreed with a manufacturer on the specific resale prices to be charged. Thus, in the absence of such

91 *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 721 (1988).

92 *Id.* at 722.

93 *Id.* at 726-27.

94 *Id.* at 727-28 ("In the vast majority of cases, it will be extremely difficult for the manufacturer to convince a jury that its motivation was to ensure adequate services, since price cutting and some measure of service cutting usually go hand in hand.").

95 *Id.* at 726.

96 *Id.* at 725.

97 *Id.* at 725-26.

98 *Id.* at 725.

an agreement, the rule of reason rather than the per se rule should apply.⁹⁹

Sharp's requirement for the setting of a specific resale price merely introduces another formalistic rule into the analysis of mixed terminations. Like the price/nonprice and unilateral/conspiracy dichotomies, the "specific price" standard bears no relationship to substantive economic effect. Indeed, the termination of a price-cutter at the behest of a competitor can have an even greater adverse effect on consumers than a manufacturer's requirement that a distributor charge a specific resale price. If Sharp had imposed resale prices and left Business Electronics and Hartwell free to compete in Houston in the nonprice arena, consumers at least could have chosen the dealer who provided the best services. As it was, however, Business Electronics was completely excluded from the relevant market. Consumers were left with only one outlet for Sharp calculators, which could set prices and provide services as it saw fit without fear of retail competition.¹⁰⁰

Terminating a distributor at a competitor's request has an indirect effect on pricing in the intrabrand market. The elimination of a competitor gives the remaining distributors greater power to control resale prices. Indeed, in *Sharp* this control was absolute, because the only other Sharp distributor in the Houston area was eliminated. The *Sharp* Court failed to acknowledge that the adverse effect on competitive pricing, though indirect, was no less than it would have been if Hartwell had agreed to charge a specific resale price.¹⁰¹ In other antitrust cases the Supreme Court has had no difficulty discerning an anticompetitive effect from conduct indirectly affecting prices.¹⁰² In *Sharp* the Court conceded that it

99 *Id.* at 727.

100 As Judge Mansfield argued in his dissenting opinion in *Oreck Corp. v. Whirlpool Corp.*, 579 F.2d 126 (2d Cir.) (en banc), cert. denied, 439 U.S. 946 (1978), the per se rule should apply in similar circumstances:

Before Oreck was terminated by the Sears-Whirlpool combination as a competing distributor, the public had the benefit of Oreck's competition, including price competition, in the marketing of Whirlpool cleaners After the termination the public could buy Whirlpool machines only from Sears at such prices as Sears might decide, unaffected by any Oreck competition.

Id. at 139.

101 Another court has recognized that "the coerced exclusion of discount rivals from the market place solely because of their pricing policies" impairs competition as much as do explicit price-fixing agreements. *Burlington Coat Factory v. Belk Bros. Co.*, 621 F. Supp. 224, 233 n.18 (S.D.N.Y. 1985).

102 See *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980) (wholesaler's agree-

had previously held that antitrust conspiracies need not set specific prices in order to be per se illegal. However, the Court distinguished its earlier cases on the ground that they involved horizontal agreements rather than the "vertical" conduct at issue in *Sharp*.¹⁰³

The *Sharp* Court was most deficient in characterizing Business Electronics' termination as vertical rather than horizontal conduct. Business Electronics was not terminated by Sharp to enforce a nonprice vertical restriction, to prevent free-riding, or to otherwise promote Sharp's effectiveness in competing against other manufacturers of electronic calculators. The only reason for Business Electronics' termination was to placate a rival dealer concerned about low-price competition.¹⁰⁴ Hartwell's ultimatum to Sharp possessed the classic characteristics of a group boycott: the exertion of pressure by a firm at one competitive level to induce a supplier not to deal with the boycott victim. In its previous group boycott cases the Court did not characterize the defendants' conduct as vertical simply because it was imposed from above.¹⁰⁵ However, in *Sharp* the Court distinguished cases such as *General Motors* and *Klor's* on the ground that they involved "horizontal combinations" at some competitive level, while only Sharp and Hartwell were involved in the termination of Business Electronics.¹⁰⁶

Under *Sharp*, the per se rule would presumably apply when two or more distributors induce a supplier to terminate a fellow

ment to stop extending credit to retailers per se illegal); *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679 (1978) (ethical canon forbidding members of organization from engaging in competitive bidding per se illegal); *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940) (competitors' agreement to buy surplus gasoline to keep prices from falling per se illegal); *Sugar Inst., Inc. v. United States*, 297 U.S. 553 (1936) (competitors' agreement to observe certain terms of sale per se illegal). As the Court stated in *United States v. General Motors Corp.*, 384 U.S. 127 (1966), "the per se rule applies even when the effect upon prices is indirect." *Id.* at 147.

103 *Sharp*, 485 U.S. at 733-34. The House Report on the Price Fixing Prevention Act acknowledges that the majority in *Sharp* failed to recognize the Court's own precedent for applying the per se rule in similar circumstances. See HOUSE REPORT at 27 (quoting Piraino, *supra* note 11, at 330).

104 Justice Stevens dissented in *Sharp*, arguing that the majority should not have presumed a procompetitive purpose for Business Electronics' termination (e.g., insuring better customer service) when Sharp had not instituted any vertical restrictions on its distributors to encourage such services. *Id.* at 740-41 (Stevens, J., dissenting); see also Rudolph J. Peritz, *A Genealogy of Vertical Restraints Doctrine*, 40 HASTINGS L.J. 511, 550-51 (1989); Steuer, *supra* note 4, at 512.

105 See *supra* notes 46-53 and accompanying text.

106 *Sharp*, 485 U.S. at 734.

distributor; however a court would have to use the rule of reason when only one distributor caused a supplier to take the same action. In making this formalistic distinction, the Court showed less economic discernment than the lower federal courts, which in the *Cernuto* line of cases had recognized the horizontal competitive substance of terminations induced by a single distributor.¹⁰⁷ Indeed, the *Sharp* Court misinterpreted its own precedent, for in *Klor's*, as in *Sharp*, only one retailer induced a supplier to take an adverse action against a competing retailer.¹⁰⁸

What could be more arbitrary than the distinction made in *Sharp* between terminations induced by single firms and "horizontal combinations?" The adverse effect on intrabrand competition was caused by Business Electronics' coerced exclusion from the Sharp electronic calculator market in Houston, not by the number of firms who convinced Sharp to effect the termination. Justice Stevens pointed out in his dissent in *Sharp* that the termination of Business Electronics was not "different in kind" from the Chevrolet dealers' coercion in *General Motors*: "Both boycotts lack any efficiency justification—they are simply naked restraints on price competition, rather than integral, or ancillary, parts of the manufacturers' predetermined distribution policies."¹⁰⁹

The distinctions courts will now have to make in "single inducement" cases illustrate *Sharp's* formalism. The per se rule will apply when the supplier and remaining distributor agree to set a specific resale price. But when should a court deem this to have occurred? There are many scenarios in which a manufacturer and its distributors may have agreed on the price level to be charged after a distributor's termination. The retailer, for example, may

107 As the court stated in *Com-Tel, Inc. v. DuKane Corp.*, 669 F.2d 404 (6th Cir. 1982):

In *Klor's*, there was only one conspiring party on the same competitive level as *Klor's*, i.e., *Broadway-Hale*. Therefore, numerosity on the same horizontal level as the boycotted party is not required. Similarly, in *General Motors* there was only one party at the manufacturer's level. The application of the group boycott theory does not turn on the number of parties in a combination; rather it is applied to prohibit the exclusionary practices inherent in a boycott which are "inconsistent with the free-market principles embodied in the Sherman Act"

Id. at 414 (citing *United States v. General Motors Corp.*, 384 U.S. 127, 146 (1966)); see also *A.H. Cox & Co. v. Star Mach. Co.*, 653 F.2d 1302, 1305 n.3 (9th Cir. 1981) ("A per se violation might be established if a manufacturer's decision to terminate a dealer was prompted by dealer coercion, either by a single dealer or by a group of dealers.").

108 See *supra* notes 46-47 and accompanying text.

109 *Sharp*, 485 U.S. at 748 (Stevens, J., dissenting).

agree to charge between \$1.00 and \$1.10 for a particular product, to charge a particular percentage over wholesale price, or to charge the same amount as in the previous year.¹¹⁰ Or the manufacturer and retailer may play a game in which the retailer suggests a certain price and the manufacturer informs the retailer whether it is close enough to the desired resale price.¹¹¹ In which of these cases have the parties agreed to set a specific resale price under the *Sharp* formulation? These distinctions have nothing to do with the economic effect of the conduct at issue, and by concentrating on them the courts will only divert their attention from more substantive concerns.

One certainty in the post-*Sharp* era is that terminated distributors will find it extremely difficult to prevail in single inducement cases. Given the sophistication of most antitrust compliance programs, there usually will be no evidence of a manufacturer's imposition of a specific resale price. As certain commentators have observed, "Under the new rule, any businessman who actually agrees on the price he will charge should be convicted of stupidity as well as price fixing."¹¹² And indeed, the lower federal courts have begun to cite *Sharp* routinely in dismissing mixed termination cases that possess the classic characteristics of a group boycott. For example, in *Toys "R" Us, Inc. v. R. H. Macy & Co.*,¹¹³ Macy's threatened to discontinue purchasing from two swimsuit manufacturers if they continued to deal with a Toys "R" Us division selling swimsuits at a twenty to twenty-five percent discount in competition with Macy's. Both firms notified Toys "R" Us that they would no longer deal with it because of the complaints from Macy's. Despite the similarities to *Klor's*, the court granted summary judgment for Macy's on the ground that Macy's had not agreed with the manufacturers to fix a specific retail price for their swimwear.¹¹⁴

Because most terminated distributors will be unable to prove under *Sharp* that a manufacturer fixed a specific resale price, they will be forced to proceed under rule of reason rather than per se theories. A distributor will thus have to show that its termination

110 See Steuer, *supra* note 4, at 527.

111 See Burns, *supra* note 75, at 29.

112 Waldman & Cuneo, *supra* note 14.

113 728 F. Supp. 230 (S.D.N.Y. 1990).

114 *Id.* at 235-36. For other cases denying liability in similar circumstances, see *Bailey's, Inc. v. Windsor Am., Inc.*, 948 F.2d 1018 (6th Cir. 1991); *Ben Elfmans Sons, Inc. v. Criterion Mills, Inc.*, 774 F. Supp. 683 (D. Mass. 1991).

had an adverse impact on competition in a relevant market. Under standard formulations of the rule of reason, such proof will be difficult, if not impossible, for most distributors.¹¹⁵

V. THE ECONOMIC CHARACTERISTICS OF MIXED TERMINATIONS

Monsanto and *Sharp* have seriously limited the ability of individual distributors to prevail in antitrust suits. As a result of these cases manufacturers will be more willing to terminate distributors who are the object of price-cutting complaints. The antitrust laws, however, are designed to protect competition, not individual competitors. The enhancement of consumer welfare, rather than the protection of small businesses, currently is viewed as the proper goal of antitrust enforcement.¹¹⁶ Thus, *Monsanto* and *Sharp* should not be criticized simply because they limit individual distributors' freedom. A different approach is only justified to protect the competitive process from general abuses that harm consumers by raising prices or reducing output.

Under the interpretation of *Monsanto* and *Sharp* currently followed by the lower federal courts, a distributor has no real remedy when its termination is induced by a competitor. Such terminations may adversely affect intrabrand competition by increasing retail prices and limiting point-of-sale services. If the courts intend to follow an economics-based approach to antitrust policy, they should adopt a new method of analyzing mixed terminations.

A. *The Benefits of Intrabrand Competition*

Any approach to mixed terminations should recognize that intrabrand competition is worthy of protection under the antitrust laws. Although the Supreme Court stated in *Sylvania* and *Sharp*

115 See *supra* notes 20-22, 24 and accompanying text.

116 See *Rothery Storage & Van Co. v. Atlas Van Lines*, 792 F.2d 210, 228 (D.C. Cir. 1986), *cert. denied*, 479 U.S. 1033 (1987); *Polk Bros. v. Forest City Enters.*, 776 F.2d 185, 188 (7th Cir. 1985); *Valley Liquors, Inc. v. Renfield Importers*, 678 F.2d 742, 745 (7th Cir. 1982). The view that the antitrust laws should protect the freedom of individual businesses, which was in vogue in the activist antitrust era of the 1960s and early 1970s, is currently out of favor with the courts. For earlier cases stating that antitrust policy should be based on broad social goals, see *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 610 (1972) (emphasizing freedom of small business to compete); *Brown Shoe Co. v. United States*, 370 U.S. 294, 344 (1962) (pointing out the social importance of small, locally-owned businesses); *United States v. Alcoa*, 148 F.2d 416, 427 (2d Cir. 1945) (L. Hand, J.) (referring to a preference for a "system of small producers").

that "interbrand competition is the primary concern of antitrust law," the Court did not find that intrabrand competition is of no consequence.¹¹⁷ Free competition among distributors benefits consumers by reducing resale prices and encouraging marketing innovations and more efficient forms of retailing. Such competition also stimulates a greater output of services and adds to the variety and range of choices available to consumers. Because intrabrand competition is so important to consumers, a distributor termination should not be tolerated unless it potentially could cause a countervailing benefit in the interbrand market.

During the last several years, intrabrand competition has not been highly regarded by the federal courts or by economists, who have concentrated instead on the benefits of interbrand competition at the manufacturer level.¹¹⁸ However, intrabrand competition adds significant economic value at the downstream distribution level, where resellers interface directly with ultimate end-users. Distributors are more keenly aware of and better able to respond to consumers' needs and preferences than upstream suppliers. When they are allowed to compete freely, distributors are likely to develop innovative means of delivering services desired by consumers. Such innovations have included "the department store; the supermarket; the mail order firm; [and] the boutique."¹¹⁹

Competition at the resale level can reduce consumer prices and increase customer services even more effectively than interbrand competition at the supplier level.¹²⁰ There is a strong impetus toward efficiency in intrabrand markets because of the many different ways in which resale costs can be reduced. Automated purchasing and warehousing, minimization of space and in-

117 As the *Cernuto* court stated: "[I]nterbrand competition . . . has been labelled the 'primary concern of antitrust law' Nonetheless, intrabrand competition . . . has not been of so little importance as never to merit the protection of a per se rule." *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 166 n.11 (3d Cir. 1979) (citing *Continental T.V., Inc. v. GTE Sylvania Inc.* 433 U.S. 36, 52 n.19 (1977)). Justice Stevens stated in his dissent in *Sharp* that "fostering intrabrand competition has been recognized as an important goal of antitrust law." *Sharp*, 485 U.S. at 749 n.14.

118 Robert L. Steiner, *Intrabrand Competition—Stepchild of Antitrust*, 36 ANTITRUST BULL. 155, 177 (1991).

119 Department of Justice Antitrust Division: *Oversight Hearings Before Subcomm. on Monopolies and Commercial Law of the House Comm. on the Judiciary*, 99th Cong., 1st Sess. 75 (1986). One of the most recent retail innovations has been the warehouse-type "super store" that provides one-stop shopping for a variety of items at discount prices. See Isadore Barmash, *Down the Scale With the Major Store Chains*, N.Y. TIMES, Feb. 2, 1992, at F5.

120 Steiner, *supra* note 118, at 177.

ventory, management of receivables and payables, training and selection of employees, control of rental, utility, and other overhead expenses, and even the setting of store hours—all of these factors affect distributors' relative efficiency. The most efficient dealers will be able to gain a significant cost advantage over their rivals. As a result, they will be able either to offer substantial discounts or to afford greater point-of-sale services than their competitors. In response to competition from the most efficient dealers, other distributors will be forced to lower their prices or to increase their level of customer services.

It has become fashionable in recent years to apply the pejorative "free-rider" label to discounters. Discount retailers, however, are among the most innovative and efficient deliverers of products to consumers. Their cost-saving methods allow them to provide the lowest possible retail prices. Consumers have come to rely increasingly in recent years on low-price retailers. Outlet malls, superstores, mail order firms, warehouse clubs, and other discount dealers have captured an ever greater portion of the retail market. As a consumer advocate has pointed out, "during [the] current recessionary period, [discounters] are not just an option but are a salvation, offering a way to buy goods that many consumers could not afford at [the] suggested retail price."¹²¹ Indeed, one economic study has indicated that consumers pay as much as thirty percent less in discount stores than at full-price competing outlets.¹²²

In certain cases, intrabrand discounting can even reduce prices in the interbrand market. When discounting of one brand is prevalent, distributors of other brands may exert pressure on their suppliers to lower wholesale prices so that they can remain competitive with the discount brand. This phenomenon occurred in the jeans industry after Levi Strauss eliminated resale price restrictions on its distributors. Levi Strauss abandoned the restrictions in

121 *Vertical Price Fixing: Hearings Before the Subcomm. on Antitrust and Restraint of Trade Activities Affecting Small Business of House Comm. on Small Business*, 98th Cong., 1st Sess. 48 (1983) (statement of Barbara F. Warden, Executive Director, National Consumers' League). It has been estimated that "discounters now account for more than 40 percent of general merchandise business and one-third of apparel sales." Robert D. Hershey, Jr., *Tales of the Tightfisted Consumer*, N.Y. TIMES, July 4, 1992, at 31. Even upscale consumers are now seeking out discount outlets for the bargain purchase of luxury products such as BMWs, Yves Saint Laurent lipstick, and Calvin Klein perfumes. See Gretchen Morgenson, *Save \$35 on Chanel*, FORBES, March 16, 1992, at 70.

122 Doherty, *supra* note 29, at 989 n. 210.

1977 because of an impending enforcement action by the Federal Trade Commission.¹²³ Soon thereafter, a number of discount outlets reduced their prices on Levis. These price cuts triggered reductions in the prices of competing brands of jeans.¹²⁴ Similarly, after Sealy eliminated its exclusive territories and resale price restrictions for distributors of its mattresses, the prices paid by consumers for Sealy mattresses fell by as much as twenty to thirty percent. In response, competing mattress manufacturers were forced to reduce their prices.¹²⁵

The anticompetitive effect of a distributor termination is thus particularly acute when the terminated distributor is a discounter. Price-cutting distributors provide an important price alternative to consumers and a strong impetus to the efficiency of competing distributors. However, the termination of a full-price distributor can also have a significant adverse effect on intrabrand competition. Distributors often elect to compete on the basis of service as well as price.¹²⁶ Consumers may be willing to pay a higher price to distributors that provide effective product explanations, demonstrations, repairs, and other point-of-sale services. Indeed, warranty repairs of VCRs and other home electronics equipment account for more than half of many dealers' business today.¹²⁷ Distributors who can provide such point-of-sale services while maintaining market prices may be just as efficient competitors as discounters. The termination of such a service-oriented dealer reduces consumers' choices and can represent as great a loss to intrabrand competition as the termination of a discounter.

Consumer welfare is thus harmed whenever a distributor is terminated. If the terminated distributor is a discounter, resale prices are likely to rise because incumbent distributors have less incentive to match the efficiencies of a low-cost retailer. If the

123 Steiner, *supra* note 118, at 187.

124 Gerla, *supra* note 44, at 6-7.

125 Steiner, *supra* note 118, at 187. One commentator recently described how intrabrand competition can reduce interbrand prices: "the retailers look to the manufacturers to provide them with the margin dollars that consumers won't." Bill Saporito, *Why the Price Wars Never End*, FORTUNE, Mar. 23, 1992, at 68, 70.

126 Indeed, "price" has been defined in economic terms as "a shorthand for a value that includes a product and associated service." Betty Bock, *An Economist Appraises Vertical Restraints*, 30 ANTITRUST BULL. 117-23 (1985); see also M. Laurence Popofsky & Stephen V. Bomse, *From Sylvania to Monsanto: No longer a "Free Ride,"* 30 ANTITRUST BULL. 67, 88 (1985).

127 David J. Jefferson, *Service Dealers Complain About Warranty Business: Suit Against Big Electronics Concerns Cites Unprofitable Repair Work*, WALL ST. J., Feb. 20, 1992, at B2.

terminated distributor provided a high level of services, the remaining distributors will not be as compelled to develop innovative methods of customer assistance. In either case the consumer will suffer. The only beneficiary of the termination will be the inducing distributor, who will be free to set its own level of prices and services without fear of competition from its former rival.

*B. The Economic Distinction Between "Horizontal"
and "Vertical" Terminations*

Intrabrand competition is reduced regardless of whether a termination is initiated by a supplier or competing distributor. The overall competitive effect of the termination, however, varies greatly depending on the source of the termination. Manufacturers and competing distributors have entirely different competitive purposes for another distributor's termination. The origin of a distributor's termination reveals whether there is any offsetting competitive benefit which compensates for the reduction of intrabrand competition that inevitably follows the termination.

1. "Vertical" Terminations

When a manufacturer acts independently to restrict intrabrand competition, its goal invariably is to make its products more competitive against other brands. A manufacturer has a natural interest in making its products as attractive to consumers as possible. Because manufacturers ignore consumer preferences at their own peril, they will be inclined to continue to deal with the types of dealers favored by consumers. If consumers prefer to buy through low-priced outlets, a manufacturer will ultimately have to deal with discounters or suffer a general decline in demand for its products.¹²⁸ If consumers prefer higher service dealers, the manufacturer must respond by encouraging point-of-sale assistance.

A manufacturer benefits by delivering products to the ultimate end-user at the lowest possible cost. A supplier does not want to share any greater portion of its profits with its distributors than is necessary.¹²⁹ Restraints on intrabrand competition tend to divert

¹²⁸ For example, since discounters have become so popular with consumers, manufacturers of upscale cosmetics (such as Calvin Klein) have been forced to deal with outlet stores as well as with department stores. Morgenson, *supra* note 121, at 70-71.

¹²⁹ As the Court stated in *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1978):

a larger portion of this margin to distributors by increasing resale prices. Thus, a manufacturer will restrict intrabrand competition only when it believes that higher resale prices will allow distributors to increase services in a way that will make its products more attractive to consumers. The manufacturer must be careful to maintain the right mix of resale prices and services desired by consumers. The manufacturer will be forced to change its policy if it misreads consumer preferences and restricts intrabrand competition to such an extent that resale price increases reduce the overall demand for its products.¹³⁰ As the Supreme Court recognized in *Sylvania*, the manufacturer's desire to insure its competitiveness in the interbrand market will act as a natural check on its limitation of intrabrand competition.¹³¹

A natural system of checks and balances thus insures the beneficial impact of distributor terminations independently effected by suppliers. A manufacturer can be relied upon to pursue its own self-interest in minimizing the adverse competitive effect of a distributor termination. A manufacturer would not proceed on its own with a termination whose only effect was to reduce intrabrand competition and increase retail prices. When a manufacturer independently decides to terminate a distributor, and thus to reduce intrabrand competition, it can safely be assumed that it expects, in return, some offsetting benefit to consumers in the form of increased services.

2. "Horizontal" Terminations

In effecting distributor terminations, suppliers are more likely to be acting to promote their own interbrand competitiveness than simply "knuckling under" to the anticompetitive demands of their distributors. In most termination cases, distributors' complaints

Generally a manufacturer would prefer the lowest retail price possible, once its price to dealers has been set, because a lower retail price means increased sales and higher manufacturer revenues . . . a manufacturer is likely to view the difference between the price at which it sells to its retailers and their price to the consumer as its "cost of distribution," which it would prefer to minimize.

Id. at 56 n.24 (citations omitted).

130 See *Westman Comm'n Co. v. Hobart Int'l*, 796 F.2d 1216, 1226-27 (10th Cir. 1986); Robert H. Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division*, 75 YALE L.J. 373, 403 (1966); Burns, *supra* note 75, at 12; David F. Shores, *Vertical Price Fixing and the Contract Conundrum: Beyond Monsanto*, 54 FORDHAM L. REV. 377, 401 (1985).

131 *Sylvania*, 433 U.S. at 56.

simply bring to a supplier's attention deficiencies in another distributor's performance (such as poor customer service) that give the supplier adequate cause to proceed with the termination on its own. A distributor rarely possesses enough market power to convince its supplier to terminate another distributor that the supplier would have preferred to retain.¹³² However, there are cases in which a supplier, faced with an ultimatum from a dealer, may choose to proceed with a termination it otherwise would have foregone.¹³³ Preferring to keep both dealers, the supplier nevertheless may conclude that "terminating the plaintiff hurts him less (considering sales lost, transaction costs in finding and perhaps training a replacement, and any spillover effects upon his relations with other dealers) than losing the complainer's patronage."¹³⁴ This may be particularly true when the complaining distributor purchases a significantly larger volume of products from the supplier than the terminated distributor.

When one distributor induces a supplier to terminate another distributor, a different competitive purpose prevails than in the case of a vertical termination. Unlike a manufacturer, a dealer is not motivated to enhance interbrand competition but usually is driven solely by a desire to restrict intrabrand competition as much as possible in order to protect its profit margins.¹³⁵ In the

132 The Supreme Court in *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717 (1988), recognized that "[r]etail market power is rare, because of the usual presence of interbrand competition and other dealers." *Id.* at 727 n.2 (citing *Sylvania*, 433 U.S. at 54). Indeed, a manufacturer easily can refuse to participate in a dealer's termination scheme. Because the dealer usually is dependent on the manufacturer for its supply and likely has invested substantial resources in promoting the manufacturer's product, the dealer has powerful incentives not to follow through on a threat to stop selling the manufacturer's product. Even if it does so, manufacturers often easily can find substitute distributors at the unconcentrated retail level where entry barriers are low. See Kevin J. Arquit, *Market Power in Vertical Cases*, 60 ANTITRUST L.J. 921, 927 (1992) ("[C]ollusion is unlikely to succeed because retailing in many industries is a highly competitive, low-margin business, with low barriers to entry.").

133 Such a termination, in fact, occurred in *Sharp*. See *supra* notes 91-92 and accompanying text.

134 7 PHILLIP AREEDA, ANTITRUST LAW ¶ 1457a-1457b, at 166-67 (1986 & Supp. 1988).

135 As Professor Areeda has stated:

From the policy viewpoint, it can matter greatly whether manufacturer or dealer interests are being served. The former is more likely to seek efficient distribution, which stimulates interbrand competition; the latter is more likely to seek excess profits, which dampen intrabrand competition. Accordingly, antitrust policy can be more hospitable toward manufacturer efforts to control dealer prices, customers, or territories than toward the efforts of dealers to control their competitors through the manufacturer.

case of an induced distributor termination, "the harm to intrabrand competition . . . is both immediate and apparent, with no countervailing stimulation of interbrand competition, the usual saving grace of a vertical restraint."¹³⁶ In such an event, a distributor may be terminated not because it failed to provide adequate customer services, but because it had lower prices, was more efficient, or was more adept than the instigating distributor at sensing and responding to consumer preferences.

Distributor terminations that originate with competing distributors amount to naked restraints of trade whose only purpose is to suppress intrabrand competition. No conceivable efficiency-enhancing objective exists for an induced termination. If the termination were necessary to ensure more effective promotion of its products, the supplier would have terminated the distributor on its own. The only purpose of an induced termination is to free a distributor from competing with a more efficient rival. Induced terminations are most similar in effect to the types of horizontal price-fixing agreements and territorial allocations that the courts have deemed *per se* illegal.¹³⁷ Like such horizontal agreements, induced terminations eliminate a beneficial rivalry that otherwise would exist between direct competitors. Indeed, terminations induced by competing distributors have more severe anticompetitive consequences than actions taken under horizontal dealer cartels. Cartels are difficult to maintain for a long period of time. Cartel members are likely to attempt to cheat on agreements requiring them to maintain particular prices or to remain in certain territories.¹³⁸ After such cheating begins, cartels usually unravel quickly.

Id. at 167; see also *Girardi v. Gates Rubber Co.*, 325 F.2d 196, 200 (9th Cir. 1963) ("[I]t is normally the competitor who is being hurt by price-cutting who is likely to seek coercive action against the competitor who is hurting or likely to hurt him."); *Arnold Pontiac-GMC, Inc. v. General Motors Corp.*, 700 F. Supp. 838, 841 (W.D. Pa. 1988) ("A horizontal agreement by dealers . . . is only motivated by the dealers [sic] desire to eliminate intrabrand competition within the region and thereby to maximize profits. Such agreements have no procompetitive motivation, and are consistently found illegal *per se*." (citing *Piraino*, *supra* note 11, at 298).

136 *Oreck Corp. v. Whirlpool Corp.*, 579 F.2d 126, 141 (2d Cir.) (en banc) (Mansfield, J., dissenting), *cert. denied*, 439 U.S. 946 (1978).

137 See, e.g., *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980) (horizontal price-fixing by beer wholesalers); *United States v. Topco Assocs., Inc.*, 405 U.S. 596 (1972) (territorial allocation by grocery stores selling "Topco" brand).

138 In *Sharp*, the Supreme Court stated: "Cartels are neither easy to form nor easy to maintain. Uncertainty over the terms of the cartel, particularly the prices to be charged in the future, obstructs both formation and adherence by making cheating easier." *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 727 (1985) (citing *Matsushita Elec.*

Distributor terminations, however, eliminate intrabrand competition irrevocably. Once a distributor induces a manufacturer to terminate a rival, the distributor need not fear competition from that rival ever again.

The manufacturer's participation gives a mixed termination conspiracy the ability to effectively foreclose intrabrand competition. The adverse competitive effect results from a distributor's ability to enlist the supplier's participation in the conspiracy, not from the number of distributors who originate the scheme.¹³⁹ The number of distributors that induce the termination is without competitive significance. A termination induced by a single distributor can adversely affect intrabrand competition to the same extent as a termination induced by a group of distributors. Indeed, a single large distributor may have a greater ability to compel the supplier's participation than a group of smaller distributors.

Any approach to mixed terminations, then, should recognize certain economic facts: that intrabrand competition should be protected because it benefits consumers by reducing resale prices and increasing customer services; that any distributor termination adversely affects intrabrand competition; that when suppliers independently effect terminations, the beneficial impact on interbrand competition justifies the adverse effect on intrabrand competition; and that, in those rare cases where one or more distributors induce their supplier to terminate another distributor, there is no such beneficial effect on interbrand competition, but only harm to consumers from increased resale prices and reduced point-of-sale services.

Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 590 (1986); *Maple Flooring Mfrs. Ass'n v. United States*, 268 U.S. 563 (1925); *Cement Mfrs. Protective Ass'n v. United States*, 268 U.S. 588 (1925)).

139 The Supreme Court recognized in cases such as *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959), and *United States v. General Motors, Corp.*, 384 U.S. 127 (1966), that the competitive evil of a group boycott stems from the elimination of a competitor from the intrabrand market at the instigation of a rival and not from a broad horizontal conspiracy. See *supra* notes 46-50 and accompanying text.

One commentator has pointed out that "[a] dealer's success in using the refusal-to-deal weapon to strike at a competitor depends on enlisting the cooperation of their mutual supplier, not other competing dealers." Comment, *Vertical Agreement as Horizontal Restraint: Cernuto, Inc. v. United Cabinet Corp.*, 128 U. PA L. REV. 622, 641-42 (1980).

VI. A SUGGESTED ANTITRUST ANALYSIS FOR MIXED TERMINATIONS

A. *The Horizontal/Vertical Dichotomy*

The economic consequences of distributor terminations thus depend upon whether the termination was effected vertically by a supplier or induced horizontally by one or more competing distributors. In order to recognize these economic effects, the courts should adopt a horizontal/vertical analysis of mixed terminations in place of the current price/nonprice dichotomy.¹⁴⁰

Under a horizontal/vertical dichotomy, the courts would no longer have to distinguish arbitrarily between "price" and "nonprice" restraints. If a manufacturer acted independently to terminate a distributor, the court would uphold the termination regardless of whether the distributor was a price cutter. As the Supreme Court recognized in *Monsanto* and *Sharp*, a manufacturer may have legitimate reasons for terminating a discounter.¹⁴¹ When a termination is effected independently, its only conceivable purpose can be to make the supplier a more effective competitor. If a manufacturer prefers to deal through higher-priced distributors who provide greater customer services, it should have that prerogative. The manufacturer should not be deterred from implementing a high service distribution policy by fear that a dis-

140 Some courts have recognized the utility of the horizontal/vertical distinction in mixed termination cases. See, e.g., *Davis-Watkins Co. v. Service Merchandise*, 686 F.2d 1190, 1197 (6th Cir. 1982) ("A determination of the source of the restraints imposed . . . will expose the purpose of such restraints."); *Id.* at 1197 n.10 ("A restraint imposed by distributors is generally for the purpose of restricting supply or price competition . . . whereas restraints imposed intrabrand by a manufacturer may be imposed for the purpose of competing more effectively in the interbrand market.") (citations omitted); see also *Big Apple BMW, Inc. v. BMW of N. Am., Inc.* 1992-2 Trade Cas. (CCH) ¶ 69,918 (3d Cir. Aug. 6, 1992); *Crane & Shovel Sales Corp. v. Bucyrus-Erie Co.*, 854 F.2d 802, 805-06 (6th Cir. 1988); *Tunis Bros. Co. v. Ford Motor Co.*, 763 F.2d 1482, 1497 (3d Cir. 1985), *vacated and remanded*, 475 U.S. 1105 (1986); *Donald B. Rice Tire Co. v. Michelin Tire Corp.*, 638 F.2d 15, 16 (4th Cir.), *cert. denied*, 454 U.S. 864 (1981); *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 168 (3d Cir. 1979); *Lovett v. General Motors Corp.*, 769 F. Supp. 1506 (D. Minn. 1991); *Arnold Pontiac-GMC, Inc. v. General Motors Corp.*, 700 F. Supp. 838, 841 (W.D. Pa. 1988).

Professor Turner has concluded that "the economic consequences of a vertical-horizontal arrangement may well vary substantially depending on where the initiative came from and . . . legal conclusions should not be made without taking this into account." Turner, *supra* note 66, at 699; see also AREEDA, *supra* note 134, ¶ 1457, at 167-68; SULLIVAN, *supra* note 50, at § 148; Erwin A. Elias, *Dealer Termination or Exclusion, Intrabrand Competition and GTE Sylvania*, 29 BAYLOR L. REV. 435, 473 (1977); Piraino, *supra* note 11; Steuer, *supra* note 4, at 523.

141 See *supra* notes 67-70, 94 and accompanying text.

counter's termination will be deemed illegal. Indeed, an approach limiting a manufacturer's right to choose the types of distributors with which it prefers to deal could ultimately eliminate intrabrand competition by encouraging suppliers to vertically integrate.¹⁴²

On the other hand, a termination induced by competing distributors should be illegal regardless of whether the supplier and distributors had a specific price-related motive. When one or more distributors convince a supplier to terminate a competitor that otherwise would have remained in the intrabrand market, consumer prices and services are adversely affected. The adverse effect is not dependent upon the remaining distributors' agreement to sell the manufacturer's product at a specific price. Nor does it depend upon the terminated distributor being a discounteer. The induced termination of a full-price dealer can be just as anticompetitive as the coerced termination of a discounteer.¹⁴³ Since induced terminations clearly are anticompetitive, a court need not determine whether the inducing distributor was motivated by the terminated distributor's low prices or by some other

142 See *Red Diamond Supply, Inc. v. Liquid Carbonic Corp.*, 637 F.2d 1001, 1006-07 (5th Cir.), *cert. denied*, 454 U.S. 827 (1981); Almarin Phillips & Joseph Mahoney, *Unreasonable Rules and Rules of Reason: Economic Aspects of Vertical Price-Fixing*, 30 ANTITRUST BULL. 99, 102 (1985). In applying the rule of reason to nonprice vertical restraints, the court in *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977), cited "the incentive for vertical integration" that would be fostered by a *per se* approach. *Id.* at 57 n.26. Vertical integration of newspaper publishing and distribution was, in fact, the consequence of the Court's application of the *per se* rule to maximum resale price maintenance in *Albrecht v. Herald Co.*, 390 U.S. 145 (1968). See David H. Marks & Jonathan M. Jacobson, *Price-Fixing: An Overview*, 30 ANTITRUST BULL. 199, 254 (1985).

143 Courts have consistently held that the horizontal exclusion of a firm from a particular market should be *per se* illegal regardless of whether price-fixing was a motive for the exclusion. See *United States v. Topco Assocs., Inc.*, 405 U.S. 596 (1972); *Timken Roller Bearing Co. v. United States*, 341 U.S. 593 (1951); *United States v. Cadillac Over-all Supply*, 568 F.2d 1078 (5th Cir.), *cert. denied*, 437 U.S. 903 (1978); *United States v. Consolidated Laundries Corp.*, 291 F.2d 563 (2d Cir. 1961). In *United States v. General Motors Corp.*, 384 U.S. 127 (1965), the Court stated, "Nor do we propose to construe the Sherman Act to prohibit conspiracies to fix prices at which competitors may sell, but to allow conspiracies or combinations to put competitors out of business entirely." *Id.* at 148.

Several commentators have concluded that horizontal market division is as great an evil as horizontal price-fixing. See, e.g., Robert Pitofsky, *The Sylvania Case: Antitrust Analysis of Non-Price Vertical Restrictions*, 78 COLUM. L. REV. 1, 10 (1978); Peter J. Monte, Comment, *Restricted Distribution After "Schwinn"*, 9 B.C. INDUS. & COM. L. REV. 1032, 1040-41 (1968); Comment, *Vertical Agreements to Terminate Competing Distributors: Oreck Corp. v. Whirlpool Corp.*, 92 HARV. L. REV. 1160, 1163 (1979). In fact, horizontal territorial allocations arguably have a greater anticompetitive effect than horizontal price-fixing. Price-fixing eliminates only price competition among competitors, but horizontal market division eliminates all competition.

aspect of its competition. The need to deter such anticompetitive conduct justifies deeming it illegal on its face.¹⁴⁴

B. Distinguishing Horizontal from Vertical Conduct

Many courts and commentators have recognized the logic of the horizontal/vertical dichotomy.¹⁴⁵ They have concluded, however, that the distinction has little practical utility because it is difficult to determine whether a supplier's or distributor's purpose prevailed in a particular case.¹⁴⁶ Nevertheless, in contrast to the price/nonprice dichotomy, the distinction between horizontal and

144 In a special circumstance, a dealer's inducement of a termination need not be illegal. The courts have recognized that the "termination of one dealer in order to grant another exclusive distribution rights in an area is generally lawful." *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 746 n.11 (1987) (Stevens, J., dissenting) (quoting *AREEDA*, *supra* note 134, ¶ 1457, at 174-75). In applying the per se rule in *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1958), the Court noted that it was not faced with "a case of . . . a manufacturer and a dealer agreeing to an exclusive distributorship." *Id.* at 212. Several courts have agreed that "a company may contract with a new distributor and as a consequence terminate its relationship with a former distributor without running afoul of the Sherman Act, even if the effect of the new contract is to seriously damage the former distributor's business." *Motive Parts Warehouse v. Facet Enters.*, 774 F.2d 380, 386-87 (10th Cir. 1985) (citing *Dart Indus. v. Plunkett Co. of Okla.*, 704 F.2d 496, 499 (10th Cir. 1983); *Burdett Sound, Inc. v. Altec Corp.*, 515 F.2d 1245, 1249 (5th Cir. 1975)); see also *Car Carriers, Inc. v. Ford Motor Co.*, 745 F.2d 1101, 1110 (7th Cir. 1984), *cert. denied*, 470 U.S. 1054 (1985); *Oreck Corp. v. Whirlpool Corp.*, 579 F.2d 126, 131-34 (2d Cir.) (en banc), *cert. denied*, 439 U.S. 946 (1978); *Packard Motor Car Co. v. Webster Motor Car Co.*, 243 F.2d 418, 420-21 (D.C. Cir.), *cert. denied*, 355 U.S. 822 (1957). But see *Zidell Explorations, Inc. v. Conval Int'l*, 719 F.2d 1465, 1469 (9th Cir. 1983) (per se rule deemed applicable when domestic distributor of valves induced foreign manufacturer to terminate plaintiff as exclusive distributor and award distributorship to itself).

The exclusive distributorship rule is justified by the fact that, when one exclusive distributor is substituted for another, even as a result of horizontal inducement from the new distributor, there is no net reduction of intrabrand competition. It is also unlikely that the new dealer would have had sufficient market power to induce the manufacturer to effect the termination of an incumbent dealer it otherwise would have retained.

145 See *supra* note 140.

146 See, e.g., *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 744 (7th Cir. 1982) (Judge Posner noted that there was a "certain unreality" in distinguishing between the possible motivations for a dealer termination.). One commentator has stated that "an approach that attempts to determine which party's interest or initiative is more fully served by the agreement encounters difficulties; for the most significant interests of the manufacturer are themselves framed in terms of the interests of the dealer." Note, *Restrictive Channels of Distribution Under the Sherman Act*, 64 HARV. L. REV. 671, 683-84 (1966); see also Joseph P. Bauer, *Per Se Illegality of Concerted Refusals to Deal: A Rule Ripe for Re-examination*, 79 COLUM. L. REV. 685, 712 (1979); Buxbaum, *supra* note 50, at 683-84; B.J. Douek, Comment, *A Proposed Rule of Reason Analysis for Restrictions on Distribution*, 47 FORDHAM L. REV. 527, 566 (1979).

vertical conduct has a rational economic basis. Therefore, the courts should be able to easily make this distinction.

The courts could simplify their task of distinguishing between horizontal and vertical conduct by separating the issue of the cause of a termination from the issue of conspiracy. Too often in mixed termination cases, the courts have confused these two issues by assuming that antitrust liability must automatically follow once a conspiracy is found. Determining the existence of an agreement, however, should be only the first step in the antitrust analysis. An offense under section 1 of the Sherman Act has two elements: (1) a contract, combination, or conspiracy and (2) an unreasonable restraint of trade.¹⁴⁷ The second element is much more important. As one judge has pointed out, courts' "mechanistic search for direct evidence of a combination diverts consideration away from the more significant issue, which is the appropriate treatment of such conduct under the antitrust laws."¹⁴⁸

Under *Monsanto*, a supplier and complaining distributor could be deemed to have a "conscious commitment to a common scheme," and thus to have conspired, if they share a desire that another distributor be terminated.¹⁴⁹ Such a shared commitment, however, reveals nothing about the competitive purpose or effect of the termination. The supplier and distributor may each have been committed to the termination for entirely different reasons. The supplier may have effected the termination to enforce a policy requiring customer services at the resale level, while the distributor may have attempted to induce the termination simply to avoid competition from a more efficient rival. Thus, a manufacturer should not be found liable simply for "agreeing" to effect a termination. In addition to determining the presence of a conspiracy, a court should consider whether the conspiracy with the inducing distributor caused the termination. If a supplier would have proceeded with a termination in any event, the conspiracy could not be the cause of the termination, and the supplier and complaining distributor should not be liable under the federal antitrust laws.¹⁵⁰

147 See Burns, *supra* note 75, at 3.

148 Edward J. Sweeney & Sons, Inc. v. Texaco, Inc., 637 F.2d 105, 131 (3d Cir. 1980) (Sloviter, J., dissenting), *cert. denied*, 451 U.S. 911 (1981).

149 Monsanto Co. v. Spray-Rite Serv. Corp., 465 U.S. 752, 765 (1983).

150 Section 4 of the Clayton Act requires the plaintiff to demonstrate that it has been "injured in his business or property by reason of anything forbidden in the antitrust laws" 15 U.S.C. § 15 (1988). Courts have construed this language to require

By separating the issue of the cause of a termination from the question of whether the parties have entered into a formal anti-trust conspiracy, the courts can concentrate on the most important issue: which party's purposes were served by effecting the termination? The ultimate competitive result of the termination depends upon whether the distributor was terminated to effect the supplier's beneficial purposes or a distributor's anticompetitive intentions. A manufacturer should not be liable if it would have effected a distributor termination for its own reasons even in the absence of complaints from other distributors. The complaints may merely inform a manufacturer of violations of its distribution policy that justify the termination. A court should hold the manufacturer liable only when it had no purpose for a termination independent of its distributors' anticompetitive desires. Thus, a court should require the terminated distributor to prove that a competing distributor's complaints were the proximate cause of its termination; that is, but for the inducement of the competitor, the manufacturer would not have proceeded with the termination.

C. *Elements of the Causation Standard*

The "but for" causation standard would not permit liability if a distributor's complaint were simply one link in a chain of events that led to a termination.¹⁵¹ A court could not find a causal connection between the complaints and the termination "merely because one follows the other."¹⁵² The terminated distributor would have to prove that another distributor's complaints were the determinative factor in its termination. In making the but for analysis, a court should assume "that that factor was present at the

a causal nexus between the plaintiff's injury and the prohibited antitrust conduct. *See, e.g.,* Hobart Bros. Co. v. Malcolm T. Gilliland, Inc., 471 F.2d 894, 901 (5th Cir.), *cert. denied*, 412 U.S. 923 (1973). Thus, there can be no antitrust liability in the absence of "some causal connection between the alleged conspiracy and the refusal to deal." *Interphoto Corp. v. Minolta Corp.*, 295 F. Supp. 711, 721 (S.D.N.Y.), *aff'd*, 417 F.2d 621 (2d Cir. 1969); *see also* Burns, *supra* note 75, at 3.

In *Big Apple BMW, Inc. v. BMW of North America, Inc.*, 1992-2 Trade Cas. (CCH) ¶ 69,918 (3d Cir. Aug. 6, 1992), the court stated that "an antitrust plaintiff must be prepared to demonstrate a causal relationship between alleged dealer complaints and a . . . [supplier's] action in order to show that the concerted action in violation of the Sherman Act is distinguishable from 'perfectly legitimate' independent conduct." *Id.* at 68,392 (citing *Monsanto*, 465 U.S. at 763-64).

151 Contrast the Price Fixing Prevention Act currently pending in Congress, under which liability would arise if a complaint was a "major cause" of a termination. *See* SENATE REPORT, *supra* note 10, at 26.

152 *Edward J. Sweeney & Sons*, 637 F.2d at 116.

time of the event, and then ask whether, even if that factor had been absent, the event nevertheless would have transpired in the same way."¹⁵³ The test thus forces a court to consider how a manufacturer would have acted in the absence of the complaints. If a supplier would have terminated the distributor had it learned of its conduct from a source other than the complaining distributor, the complaint would not be deemed the proximate cause of the termination. In such a case, the net effect on competition would be no different than if the supplier and complaining distributor had never entered into an agreement.

The but for test would be a rigorous hurdle for plaintiffs. It would thus resolve the Supreme Court's concern in *Monsanto* and *Sharp* that fear of antitrust liability deters suppliers from taking legitimate actions to encourage point-of-sale services.¹⁵⁴ This high threshold for proving causation should make manufacturers more comfortable in proceeding with terminations of distributors who are failing to provide customer services, even if that failure initially is brought to their attention by other distributors. Suppliers and distributors, then, would feel free to communicate legitimate information about their effectiveness in meeting consumer preferences.¹⁵⁵

The courts are well equipped to determine a manufacturer's purpose for a termination under a separate causal standard.¹⁵⁶ Courts are very familiar with "but for" tests, having used them for

153 *Price Waterhouse v. Hopkins*, 490 U.S. 228, 240 (1989) (construing proximate cause analysis in employment discrimination action).

154 See *supra* notes 68-71, 94 and accompanying text.

155 Such information can be very important for manufacturers:

Manufacturers rely heavily upon the "middle man," that is distributors and retailers, for information from consumers about their products: are the products too big? too small? too expensive? to [sic] few? too many?; are they properly advertised, properly constructed, etc. The distributor and retailer generally have first-hand experience with consumers and first-hand knowledge of consumer reaction to a manufacturer's products, information which the manufacturer needs to keep its product competitive in the market place.

SENATE REPORT, *supra* note 10, at 13.

156 Some courts and commentators, however, believe that it is too difficult for courts to distinguish permissible motives from illegal intent in mixed termination cases. See *Lomar Wholesale Grocery, Inc. v. Dieter's Gourmet Foods, Inc.*, 824 F.2d 582, 594 (8th Cir. 1987), *cert. denied*, 484 U.S. 1010 (1988); *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 744 (7th Cir. 1982); *Burns*, *supra* note 75, at 35; Peter M. Gerhart, *The "Competitive Advantages" Explanation for Intrabrand Restraints: An Antitrust Analysis*, 1981 DUKE L.J. 417, 439 ("Focusing on subjective motive . . . is risky and ineffectual; not only can evidence of purpose be manipulated, but the evidence is usually ambiguous.").

years in proving cause-in-fact in tort actions.¹⁵⁷ Triers of fact are accustomed to determining issues of purpose and motivation. Indeed, they are more capable of deciding such issues than resolving the complex economic problems raised in standard rule of reason cases.¹⁵⁸ The courts traditionally have recognized that "motive and intent play leading roles"¹⁵⁹ in antitrust cases. As Justice Stevens stated in his dissent in *Sharp*, "[I]n antitrust, as in many other areas of the law, motivation matters and factfinders are able to distinguish bad from good intent."¹⁶⁰ The courts have deemed purpose to be a particularly important factor in group boycott cases, where the parties may have different competitive motives for participating in the boycott.¹⁶¹

In other legal areas, courts routinely resolve cases involving mixed motives. For example, under Title VII of the Civil Rights Act of 1964,¹⁶² courts must determine whether employment decisions are based on objective standards or on such discriminatory bases as race, religion, sex, or national origin. Employers' decisions on hiring and promotion are often based on a mixture of legitimate and illegal motives.¹⁶³ Distinguishing which motive pre-

157 Gerla, *supra* note 44, at 15.

158 See *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 609-12 (1972); see also *Arizona v. Maricopa County Medical Soc'y*, 457 U.S. 332, 343 (1982). Indeed, most juries simply are incapable of performing the type of economic analysis required under a full rule of reason approach. See Burns, *supra* note 75, at 37-38.

159 *Poller v. Columbia Broadcasting Sys., Inc.*, 368 U.S. 464, 473 (1962).

160 *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 754 (1988) (Stevens, J., dissenting) (citing *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 610-11 (1985); *McLain v. Real Estate Bd. of New Orleans, Inc.*, 444 U.S. 232, 243 (1980); *United States v. Socony-Vacuum Oil Co., Inc.*, 310 U.S. 150, 224-26 n.59 (1940); *Chicago Bd. of Trade v. United States*, 246 U.S. 231, 238 (1918); Thomas A. Piraino, Jr., *The Case for Presuming the Legality of Quality Motivated Restrictions on Distribution*, 63 NOTRE DAME L. REV. 1 (1988)).

Prior to *Sharp*, the Supreme Court appeared to be moving toward an antitrust standard that emphasized a defendant's purpose in implementing competitive restraints. In *Broadcast Music, Inc. v. CBS*, 441 U.S. 1 (1979), the Court stated that a defendant's purpose for a restraint "tends to show [its] effect." *Id.* at 19. In *White Motor Co. v. United States*, 372 U.S. 253 (1963), the Court referred to the relevance of defendants' motives. *Id.* at 256-59. Finally, by emphasizing the redeeming effects of nonprice vertical restraints in *Sylvania*, the Court implicitly found purpose to be a critical factor in a Sherman § 1 analysis. *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 55 (1977).

161 One court has concluded that in all boycott cases "the touchstone of per se illegality has been the purpose and effect of the arrangement in question." *E.A. McQuade Tours, Inc. v. Consolidated Air Tour Manual Comm.*, 467 F.2d 178, 187 (5th Cir. 1972), cert. denied, 409 U.S. 1109 (1973).

162 42 U.S.C.A. § 2000 e-1 to -17 (West 1981 & Supp. 1992).

163 See, e.g., *Price Waterhouse v. Hopkins*, 490 U.S. 228, 246 (1989) (calling these "mixed motives case[s]").

dominates in a Title VII case is no more difficult than determining whether a distributor termination was motivated by a supplier's independent purposes or by a distributor's anticompetitive desires.

D. Indications of Horizontal or Vertical Cause

Most mixed terminations reveal outward indications of the parties' purpose. Thus, a court need not read a defendant's mind to determine the causal issue. In order to provide effective guidance on antitrust compliance, courts should clarify which external factors will raise an inference that the inducement of another distributor caused a termination.

For suppliers contemplating a distributor termination, the primary antitrust issue is whether a jury will consider the distributor's claim. The mere risk of a jury trial may be enough to deter a supplier from effecting a termination that could have made its products more competitive in the interbrand market. In order to protect suppliers, who most often terminate distributors for procompetitive reasons,¹⁶⁴ courts should not allow an inference of horizontal causation simply from the timing of distributor complaints. The termination of a distributor immediately after the receipt of a price-cutting complaint provides some circumstantial evidence of horizontal cause.¹⁶⁵ Standing alone, however, such evidence should not raise an inference of horizontal cause. It is natural and appropriate for a supplier to be concerned about and to react to complaints from its distributors about another distributor's competitive activities, but such conduct does not prove that a supplier had an anticompetitive purpose for a termination.

The plaintiff's case will be more persuasive if it can combine evidence on the timing of complaints with other indications of horizontal inducement. The substance of the complaints themselves often will indicate the parties' anticompetitive purpose. The complaints may reveal more than a distributor's simple dissatisfaction with a rival's discounting. The distributor may expressly request that the supplier terminate the plaintiff and may threaten to condition future purchases on the supplier's compliance. The evi-

¹⁶⁴ See *supra* note 132 and accompanying text.

¹⁶⁵ A supplier also can use the timing of complaints to rebut an inference of horizontal cause. In *Edward J. Sweeney & Sons, Inc. v. Texaco, Inc.*, 637 F.2d 105 (3d Cir. 1980), *cert. denied*, 451 U.S. 911 (1981), for example, the court failed to find liability where the complaints had commenced a full five years before a supplier took any action to terminate a distributor. *Id.* at 114.

dence of horizontal cause will be particularly strong when such an ultimatum is delivered by several distributors or by a single distributor who purchases a greater volume of products from the supplier than the plaintiff.¹⁶⁶ Such evidence should be sufficient to raise an inference that, but for the ultimatum, the supplier would not have terminated the plaintiff.¹⁶⁷

Even when the plaintiff has introduced such evidence, a supplier should have an opportunity to rebut the inference of horizontal cause by demonstrating that it had its own reasons for acceding to the threats of a distributor. A supplier should prevail on summary judgment if it can show that it terminated the plaintiff for violating a valid pre-existing distribution policy. The supplier, for example, may have had an express policy requiring distributors to provide certain customer services, or the supplier may have sought to ensure such services by precluding distributors from competing against each other for particular customers or in certain territories. A manufacturer should not be liable for terminating a distributor which fails to observe such pre-existing policies, even if the termination occurs after a threat from another distributor. Although the distributor may have anticompetitive reasons for the threat, the manufacturer may feel compelled to effect the termination to ensure the continued viability of its distribution policy.¹⁶⁸ In such a case, a terminated distributor could not meet its burden of showing that a rival's threat was the sole activating cause of its termination. Thus, if a manufacturer can prove that it had implemented territorial or customer restrictions in order to prevent free-riding, an ultimatum from the distributors requiring the manufacturer to enforce such restrictions should not give rise to antitrust liability.¹⁶⁹

166 It was an ultimatum from the larger of two competing dealers that caused the termination in *Sharp*. See *supra* notes 91, 92, 104 and accompanying text. In *Big Apple BMW, Inc. v. BMW of North America, Inc.*, 1992-2 Trade Cas. (CCH) ¶ 69,918 (3d Cir. Aug. 6, 1992), there was evidence that several dealers had been able to convince the supplier to deny the grant of an automobile dealership to a potential competitor. *Id.* at 68,939-40.

167 In *Burlington Coat Factory Warehouse v. Belk Bros.*, 621 F. Supp. 224 (S.D.N.Y. 1985), for example, a supplier was found liable for terminating a discounter after its largest distributor threatened to discontinue further purchases. *Id.* at 233.

168 For example, in *O.S.C. Corp. v. Apple Computer, Inc.*, 792 F.2d 1464 (9th Cir. 1986), Apple Computer had banned mail order sales of its computers after several of its dealers had complained of price competition from such outlets. In upholding Apple's conduct, the court relied on Apple's pre-existing marketing strategy to deal only with those distributors that could provide customer services. *Id.* at 1468.

169 When a manufacturer has implemented vertical territorial or customer restrictions

The manufacturer's evidence, however, must show that it introduced a restrictive distribution policy prior to the complaints and that it terminated the plaintiff in a legitimate effort to enforce such a policy. General after-the-fact statements about the manufacturer's concern for free-riding should not suffice.¹⁷⁰ The history of the supplier's relationship with the plaintiff and other distributors may reveal whether in fact the supplier did have a real policy prior to the time of the complaints. The supplier, for example, may have previously warned the plaintiff about violations of its distribution policy or taken actions against other distributors which committed such violations. If, on the other hand, the supplier never discussed the policy with the plaintiff prior to the termination or allowed other distributors to violate the policy with impunity, a court may be less willing to accept the supplier's argument that it acted independently.¹⁷¹

E. Elements of the Conspiracy Standard

Under the but for standard, a terminated distributor will not be able to reach a jury without substantial evidence that its supplier was motivated only by the anticompetitive concerns of a rival

to prevent free-riding, its enforcement of such restrictions following distributors' complaints does not limit intrabrand competition any more than it was already limited under the vertical restraints. See *Morrison v. Murray Biscuit Co.*, 797 F.2d 1430, 1439 (7th Cir. 1986); *McCabe's Furniture, Inc. v. La-Z-Boy Chair Co.*, 798 F.2d 323, 329-30 (8th Cir. 1986), *cert. denied*, 486 U.S. 1005 (1988); *Landmark Dev. Corp. v. Chambers Corp.*, 752 F.2d 369, 371-72 (9th Cir. 1985); *Davis-Watkins Co. v. Service Merchandise*, 686 F.2d 1190, 1200-01 (6th Cir. 1982); *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 744 (7th Cir. 1982).

170 In *Com-Tel, Inc. v. DuKane Corp.*, 669 F.2d 404 (6th Cir. 1982), the court held the manufacturer liable because the manufacturer could not show an independent reason for terminating its distributor for territorial incursions into another distributor's territory. *Id.* at 410-11. The court relied on the fact that the manufacturer had not previously implemented a program of restricted distribution. *Id.* Similarly, the majority in *Sharp* should have recognized that there was no indication that Sharp terminated the plaintiff in order to enforce its pre-existing distribution policies, rather than to simply placate a competing distributor. See *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 741 (1988) (Stevens, J., dissenting).

171 In finding the manufacturer liable in *Monsanto*, the Court referred to the fact that "Monsanto never discussed with Spray-Rite prior to the termination the distributorship criteria that were the alleged basis for the action." *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 767 (1983). In *Schwimmer v. Sony Corporation of America*, 1980-81 Trade Cas. (CCH) ¶ 63,766 (E.D.N.Y. 1981), *rev'd*, 677 F.2d 946 (2d Cir.), *cert. denied*, 459 U.S. 1007 (1982), a supplier argued that it terminated a distributor for failing to repay advertising credits rather than because of competitors' complaints. *Id.* at 78,088. The court held the supplier liable because it had not previously terminated a distributor for such conduct. *Id.*

distributor. With such a high threshold for proving causation, the courts would not have to impose a heavy burden on plaintiffs to show a conspiracy between the supplier and another distributor. Since a defendant could not be held liable without clear proof of horizontal cause, courts could feel comfortable inferring the existence of a conspiracy from circumstantial evidence.

Prior to *Monsanto*, courts had recognized that direct evidence of a conspiracy should not be required in an antitrust case because it is rarely available.¹⁷² As one judge pointed out, antitrust conspiracies "are not usually brought to light by direct evidence or frank admissions," but often require the fact finder to judge "acts . . . mostly circumstantial in nature, requiring judicious application of those inferences which arise from the conduct under scrutiny."¹⁷³ In antitrust cases, courts have traditionally deferred to the fact finder to make the ultimate determination of the inferences to be drawn from ambiguous evidence.¹⁷⁴ Thus, in several cases, the Supreme Court has been willing to infer the existence of a conspiracy from ambivalent conduct.¹⁷⁵

Monsanto does not compel courts to adopt a higher hurdle for proof of conspiracy in mixed termination cases. Indeed, contrary to the opinion of most lower federal courts,¹⁷⁶ *Monsanto* should not preclude the federal judiciary from inferring a conspiracy from circumstantial evidence. The facts of *Monsanto*, as opposed to the Court's rhetoric, support such an approach.¹⁷⁷ By engaging

172 See *McCabe's Furniture, Inc. v. La-Z-Boy Chair Co.*, 798 F.2d 323 (8th Cir. 1986), cert. denied, 486 U.S. 1005 (1988); *Terry's Floor Fashions, Inc. v. Burlington Indus.*, 763 F.2d 604 (4th Cir. 1985); *Bostick Oil Co., Inc. v. Michelin Tire Corp.*, 702 F.2d 1207 (4th Cir.), cert. denied, 464 U.S. 894 (1983).

173 *Bruce Drug, Inc. v. Hollister, Inc.*, 688 F.2d 853, 861 (1st Cir. 1982) (Torruella, J., dissenting); see also *Terry's Floor Fashions, Inc. v. Burlington Indus.*, 568 F. Supp. 205, 210 (E.D.N.C. 1983), aff'd, 763 F.2d 604 (4th Cir. 1985). In *McCabe's Furniture, Inc. v. La-Z-Boy Chair Co.*, 798 F.2d 323, 328 (8th Cir. 1986), cert. denied, 486 U.S. 1005 (1988), the court concluded that simply because "the evidence of concerted action is primarily circumstantial does not undermine this conclusion: conspiracies are rarely evidenced by explicit agreements, and therefore may be proved by circumstantial evidence and the reasonable inferences that may be drawn therefrom." *Id.* at 328.

174 See *Hospital Bldg. Co. v. Trustees of Rex Hosp.*, 425 U.S. 738, 746 (1976); *Poller v. Columbia Broadcasting Sys., Inc.*, 368 U.S. 464, 473 (1962). The fact finder plays a particularly important role in dealer termination cases, where purpose is so critical and the "evidence will often reflect what counsel advise businessmen their purpose should have been." *Pitofsky*, *supra* note 143, at 35.

175 See *United States v. Parke, Davis and Co.*, 362 U.S. 29 (1960); *American Tobacco Co. v. United States*, 328 U.S. 781 (1946); *Interstate Circuit v. United States*, 306 U.S. 208 (1939).

176 See *supra* notes 84-87 and accompanying text.

177 See *supra* notes 80-82 and accompanying text. Even Senator Metzenbaum, the

in a separate causal analysis as proposed in this Article, the courts can meet *Monsanto's* requirement for proof of "something more" than evidence of complaints in mixed termination cases.¹⁷⁸ The "something more" will consist of a plaintiff's proof, under the but for test, that a supplier was acceding to a distributor's anticompetitive desires in effecting a termination.

In the recent case of *Eastman Kodak*,¹⁷⁹ the Supreme Court exploded the notion held by many commentators and lower federal courts since *Monsanto*¹⁸⁰ that antitrust plaintiffs must meet a higher threshold of proof in order to survive a summary judgment motion. The Court specifically stated that its prior precedent "did not introduce a special burden on plaintiffs facing summary judgment in antitrust cases."¹⁸¹ According to the Court, the plaintiff need not disprove any arguments advanced by the defendant, but simply must present evidence from which "reasonable inferences" supporting its claims can be drawn.¹⁸²

The federal courts, therefore, should be willing to infer an illegal conspiracy when the circumstances surrounding a distributor termination reveal a reasonable possibility that, as required by *Monsanto*, the parties had a "conscious commitment to a common scheme."¹⁸³ Obviously, the manufacturer's commitment to the scheme is indicated by its proceeding with the termination. A

sponsor of the Consumer Protection Against Price-Fixing Act of 1991, S. 429, 102d Cong., 1st Sess. (1991), in the Senate, concedes that the problem with *Monsanto* lies not with the Court's holding, but with the lower federal courts' interpretation of its conspiracy standard. See 60 Antitrust & Trade Reg. Rep. (BNA) No. 1515, at 652 (May 9, 1991). In fact, in the post-*Monsanto* era, some lower federal courts have been willing to find an illegal agreement even in the absence of direct evidence of a conspiracy. See *supra* cases cited in note 90. In the recent case of *ES Development, Inc. v. RWM Enterprises, Inc.*, 939 F.2d 547 (8th Cir. 1991), *cert. denied*, 112 S. Ct. 1176 (1992), the court inferred a conspiracy from the parallel action of several automobile dealers who complained in concert to manufacturers about the planned location of additional dealerships at a nearby "automobile mall." *Id.* at 554. The court stated that "it is axiomatic that the typical conspiracy is rarely evidenced by explicit agreements, but must almost always be proved by inferences that may be drawn from the behavior of the alleged conspirators." *Id.* at 553 (quotations omitted).

178 See *supra* note 72 and accompanying text.

179 112 S. Ct. 2072 (1992).

180 See *supra* notes 84-87 and accompanying text.

181 *Eastman Kodak*, 112 S. Ct. at 2083.

182 *Id.* The Court's decision in *Eastman Kodak* has already been used in the Court of Appeals as authority for allowing a terminated dealer to survive a supplier's motion for summary judgment. See *Big Apple BMW, Inc. v. BMW of N. Am., Inc.*, 1992-2 Trade Cas. (CCH) ¶ 69,918, at 68,991 (3d Cir. Aug. 6, 1992).

183 See *supra* note 72 and accompanying text.

court, therefore, should limit its inquiry to whether the complaining dealers shared the desire that the plaintiff be terminated. An outright demand for termination would be proof of the dealers' intent to join the manufacturer in the termination scheme. Proof of the dealers' commitment may also arise from more circumstantial evidence. For example, frequent complaints or meetings between the manufacturer and dealers immediately prior to the termination may indicate that the dealers intended that a rival be terminated.

F. Fairness of the Proposed Standard

The standard for distinguishing horizontal from vertical conduct proposed in this Article is fair to both suppliers and distributors. Since the plaintiff has a high threshold of proof under the but for standard, suppliers will not be liable when they independently effect terminations designed to maintain the integrity of their distribution systems. With a renewed emphasis by the courts on purpose and motive, suppliers will be able to protect themselves from the costs and risks of a jury trial by documenting, in advance, their beneficial vertical intent for particular terminations.

Terminated distributors also will be better served by the courts' emphasis on the substantive competitive purpose for terminations. Plaintiffs' claims will no longer be subject to dismissal on grounds divorced from the economic effects of the terminations. Freed of the price/nonprice dichotomy, a terminated distributor will not have to prove a direct effect on resale prices, but simply that a competitor induced its termination. Plaintiffs' claims will not be barred from consideration at trial when direct evidence of a conspiracy between a supplier and complaining distributors is lacking. Finally, since an inducing distributor as well as the supplier will be liable when the but for test is met, distributors will be assured that their rivals will be deterred from originating anticompetitive termination schemes.

VII. RECONCILING THE NEW APPROACH WITH RECENT SUPREME COURT PRECEDENT

The causal analysis proposed in this Article is an effective means of distinguishing procompetitive vertical terminations from anticompetitive horizontal ones. The question remains, however, whether the lower federal courts are free to adopt such an analysis under recent Supreme Court precedent. There are two impedi-

ments to the adoption of the approach proposed in this Article: the price/nonprice dichotomy that resulted from the *Sylvania* decision and *Sharp's* severe limitation on the per se analysis in mixed termination cases.¹⁸⁴

A. An "Ancillary Restraints" Approach

A form of antitrust analysis adopted long before the *Sharp* or *Sylvania* decisions provides a method by which the lower federal courts can utilize the horizontal/vertical distinction in place of the price/nonprice dichotomy. In 1898, Judge Taft first set forth the "ancillary restraints" doctrine in *United States v. Addyston Pipe and Steel Co.*¹⁸⁵ In that case, Judge Taft held that a restraint of trade should be permissible when it was "ancillary to the main purpose of a [lawful] contract [and] was reasonably adapted and limited to the necessary protection of a party in the carrying out of such purpose"¹⁸⁶ This approach provides a simple and effective means of distinguishing between permissible and illegal restrictions on competition. Under Judge Taft's analysis, restrictions necessary to promote a procompetitive objective would be allowed; however, "naked" restraints of trade unrelated to any legitimate competitive purpose would be void.

Until recently, courts largely neglected the ancillary restraints doctrine. However, the federal courts have revived this approach during the last decade. In several recent cases, the lower federal courts used the ancillary restraints doctrine to uphold horizontal competitive restrictions rather than subject them to the per se rule. The courts concluded that the restrictions were necessary to ensure the effectiveness of cooperative arrangements designed to promote, rather than to restrict, competition.¹⁸⁷

184 See *supra* notes 25-35, 93-99 and accompanying text.

185 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

186 *Id.* at 283.

187 See *National Bancard Corp. v. VISA U.S.A., Inc.*, 779 F.2d 592, 601-02 (11th Cir.) (denying application of per se rule to interchange fee among members of VISA credit card system because fee was "'necessary' term without which the system would not function"), *cert. denied*, 479 U.S. 923 (1986); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 229 (D.C. Cir. 1986) (upholding horizontal restraints among agents of van line designed to avoid free riding), *cert. denied*, 479 U.S. 1033 (1987); *Polk Bros. v. Forest City Enters., Inc.*, 776 F.2d 185, 188 (7th Cir. 1985) (applying rule of reason to noncompetition covenant between competing dealers that was designed to eliminate free riding).

Although the Supreme Court has not yet expressly adopted the ancillary restraints doctrine, it has implicitly followed the approach on a few occasions. In those cases, the Court declined to use the per se rule when horizontal agreements were implemented in connection with legitimate cooperative endeavors. For example, in *Broadcast Music, Inc. v. CBS*,¹⁸⁸ members of a musical composers association had agreed on a common price for the licensing of their musical compositions. If the Court had followed its traditional approach to price-related restraints, it would have found this arrangement illegal on its face.¹⁸⁹ Indeed, the Court conceded that the scheme constituted price-fixing "in the literal sense."¹⁹⁰ Nevertheless, the Court upheld the arrangement because it was critical to the achievement of the composers' procompetitive purpose: the effective marketing of their musical compositions.¹⁹¹ In *Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co.*,¹⁹² the plaintiff argued that its expulsion from a purchasing cooperative of office supply stores constituted a per se illegal group boycott. The Court, however, refused to apply its traditional per se approach, pointing out that the cooperative promoted purchasing efficiencies for the stores and, without reasonable membership rules, could not operate effectively.¹⁹³

Broadcast Music and *Northwest Wholesale* indicate that the Court may be willing to use an ancillary restraints analysis to uphold restrictions that are necessary to ensure the effectiveness of cooperative ventures that have a procompetitive purpose. Under the Court's standard approach, the price-fixing in *Broadcast Music* and the group boycott in *Northwest Wholesale* would have been found illegal on their face. However, in each case, the Court looked beyond the outward form of the arrangement and considered the parties' competitive intent. The Court upheld the restraints at issue because they were essential to the operation of partnerships designed to promote, rather than to restrict, competition. In *Broadcast Music*, the composers had formed a joint venture that

188 441 U.S. 1 (1979).

189 Horizontal price-fixing had traditionally been considered by the Court to be the most firmly established of all per se illegal conduct. See, e.g., *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679, 695 (1978); *United States v. Container Corp. of Am.*, 393 U.S. 333, 337 (1969); *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 224 (1940); *Sugar Inst. v. United States*, 297 U.S. 553, 601-05 (1936).

190 *Broadcast Music*, 441 U.S. at 8.

191 *Id.* at 21, 24.

192 472 U.S. 284 (1985).

193 *Id.* at 295, 298.

made their compositions more readily available to the public,¹⁹⁴ and, in *Northwest Wholesale*, the stationery stores created a cooperative that allowed smaller retailers to compete more effectively.¹⁹⁵

The ancillary restraints analysis, implicitly adopted by the Court in *Broadcast Music* and *Northwest Wholesale*, provides a basis for upholding all vertical terminations. Like the license agreements in *Broadcast Music* and the membership rules in *Northwest Wholesale*, vertical terminations effected independently by suppliers are ancillary to a procompetitive cooperative arrangement; that is, the partnership between a supplier and its distribution network to promote interbrand competition.¹⁹⁶ In an economic sense, a supplier is engaged in a joint venture with its distributors to deliver products to consumers in the most efficient manner possible. As long as a supplier makes a termination decision in order to promote the effectiveness of its distribution system, it should not matter whether the termination was motivated by "price" or "nonprice" concerns. The termination should be upheld in any event because it is ancillary to the supplier's legitimate desire to increase its effectiveness in the interbrand market.¹⁹⁷

An ancillary restraints analysis also requires that terminations induced by one or more competing distributors be deemed illegal. Induced terminations are unrelated to any legitimate competitive purpose. Unlike the parties to the cooperative arrangements at issue in *Broadcast Music* and *Northwest Wholesale*,¹⁹⁸ distributors of a particular brand are not engaged in a procompetitive partnership with each other. The partnership designed to promote interbrand competition is vertically directed by the supplier, not horizontally imposed by distributors. Distributors are not motivated by an intent to further competition with other brands, but by a

194 *Broadcast Music*, 441 U.S. at 20.

195 *Northwest Wholesale*, 472 U.S. at 295.

196 Some commentators have compared this relationship to a partnership. See Bork, *supra* note 130, at 404; Liebler, *supra* note 36, at 906 n.80.

197 In fact, some courts have used the ancillary restraints doctrine to uphold resale price restrictions implemented by a manufacturer in conjunction with nonprice restraints. See *McCabe's Furniture, Inc. v. La-Z-Boy Chair Co.*, 798 F.2d 323 (8th Cir. 1986), *cert. denied*, 486 U.S. 1005 (1988); *Morrison v. Murray Biscuit Co.*, 797 F.2d 1430 (7th Cir. 1986); *Jack Walters & Sons v. Morton Bldgs., Inc.*, 737 F.2d 698 (7th Cir.), *cert. denied*, 469 U.S. 1018 (1984); *Eastern Scientific Co. v. Wild Heerburg Instruments*, 572 F.2d 883 (1st Cir.), *cert. denied*, 439 U.S. 833 (1978). Some commentators have argued that resale price restraints should be upheld as ancillary to a manufacturer's procompetitive partnership with its distributors. See, e.g., BORK, *supra* note 36, at 29.

198 See *supra* notes 188-95 and accompanying text.

desire to increase their individual profits in the intrabrand market. The surest route to such an increase is by eliminating competition from a rival. Thus, termination schemes that originate with distributors are not ancillary to a legitimate procompetitive arrangement, but are simply naked restraints of trade designed to suppress competition. Under *Addyston Pipe*, *Broadcast Music*, and *Northwest Wholesale*, courts should deem distributor-induced terminations illegal on their face because their only purpose is to restrict competition.

B. A New Rule of Reason Approach for Mixed Terminations

Can an ancillary restraints analysis still be applied to all distributor terminations after *Sharp*? In *Sharp*, the Court required the terminated distributor to use a rule of reason, rather than a per se, approach because a single competitor induced its termination.¹⁹⁹ Under a traditional rule of reason analysis, the terminated distributor has to prove more than an anticompetitive purpose for its termination; it also faces the nearly impossible task of showing that its termination caused an adverse impact on interbrand competition.²⁰⁰ A closer reading of *Sharp* and other recent Supreme Court cases, however, reveals that a distributor termination induced by one or more competitors can be deemed illegal without a market analysis.

In recent years, some federal courts have begun to recognize that the alternative to the per se rule need not be a traditional rule of reason market analysis. These courts have used a more abbreviated rule of reason approach that focuses simply on the defendant's purpose for implementing a competitive restraint.²⁰¹ This new standard, rather than the traditional market-based rule of reason, could be used as the alternative approach mandated by the Court in *Sharp*. Under this new standard, no further inquiry would be necessary once the plaintiff proved that its termination was in response to the anticompetitive concerns of one of its rivals. Since an induced termination has no redeeming beneficial effect on interbrand competition, its restriction of intrabrand competition would suffice to prove its illegality.

It is legitimate for courts to give prominent consideration to intrabrand competition under a new rule of reason standard. *Sylvania* and *Sharp* stated that interbrand competition is the "pri-

199 See *supra* notes 91-99 and accompanying text.

200 See *supra* note 44 and accompanying text.

201 See *infra* notes 220-43 and accompanying text.

mary concern" of antitrust law,²⁰² but they did not state that it was the only concern. Several lower federal court cases decided after *Sylvania* have held that restrictions that affect only intrabrand competition can be found illegal without a market analysis.²⁰³

In *Eastman Kodak*, the Supreme Court recognized that the suppression of intrabrand competition can be illegal in itself. Eastman Kodak had adopted a policy under which it would only sell replacement parts to those purchasers of its copiers who would also agree to have Kodak repair the copiers.²⁰⁴ As a result of this policy, independent service organizations ("ISOs"), which had previously repaired Kodak copiers in competition with Kodak, were forced out of business. There was evidence that the ISOs had supplied repair services at a lower price than Kodak.²⁰⁵ Kodak moved for summary judgment on the ISOs claim that Kodak had illegally tied the sale of its replacement parts to its repair services. In denying Kodak's motion, the Court determined that the after-market sales of parts and services for Kodak copiers were separate markets for purposes of the tying analysis.²⁰⁶ Kodak could be found per se liable at trial if the plaintiffs could prove that Kodak had used its market power in the parts market to force customers to purchase repair services from it.²⁰⁷ In a significant footnote, the Court emphasized its concern for the unjustified restriction of intrabrand competition.²⁰⁸ The Court pointed out that it had not been unduly concerned about the limitation of intrabrand competition in *Sylvania* because the parties in that case were in a vertical relationship.²⁰⁹ In *Eastman Kodak*, the concern for intrabrand competition was greater because "[i]n the relevant market, service, Kodak and the ISOs are direct competitors; their relationship is horizontal."²¹⁰ The Court concluded that, by "repeating the mantra 'interbrand competition,'" Eastman Kodak could not

202 *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 726 (1988); *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 52 n.19 (1977).

203 See, e.g., *Eiberger v. Sony Corp.*, 622 F.2d 1068 (2d Cir. 1980); *New York v. Anheuser-Busch, Inc.*, 673 F. Supp. 664 (E.D.N.Y. 1987); *Redwood Theatres, Inc. v. Festival Enters., Inc.*, 248 Cal. Rptr. 189 (Cal. Ct. App. 1988).

204 *Eastman Kodak Co. v. Image Technical Servs.*, 112 S. Ct. 2072 (1992).

205 *Id.* at 2077.

206 *Id.* at 2079-80.

207 *Id.* at 2081.

208 *Id.* at 2084 n.18.

209 *Id.* at 2084-85 n.18.

210 *Id.* at 2084 n.18.

obviate the adverse effect of its conduct in the intrabrand market for servicing Kodak copiers.²¹¹

In *Eastman Kodak*, the Court thus recognized that the effect on intrabrand competition can be particularly adverse when horizontal conduct is involved and, indeed, that the per se rule should apply when one competitor is able to eliminate its rivals from the intrabrand market. The rationale of *Eastman Kodak* suggests that it should be illegal for one or more distributors to induce a supplier to terminate a competitor. Such conduct affects intrabrand competition as adversely as Kodak's exclusion of the ISOs from the copier repair market.

The question remains, however, whether these implications of *Eastman Kodak* can be reconciled with *Sharp*. It is easy to reconcile *Eastman Kodak* with *Sharp* when more than one distributor induces a supplier to terminate a rival. In *Sharp*, the Court expressly reaffirmed its prior holdings in *Klor's*, *General Motors*, and *Topco* on the per se illegality of broad horizontal restrictions of intrabrand competition.²¹² In fact, in the recent case of *Lovett v. General Motors Corp.*,²¹³ the court construed *Sharp* to require that distributor terminations induced by a group of competitors be found per se illegal as naked restrictions of intrabrand competition.²¹⁴

211 *Id.*

212 In fact, the Court used language that supports using a horizontal/vertical dichotomy to analyze distributor terminations:

This notion of equivalence between the scope of horizontal *per se* illegality and that of vertical *per se* illegality was explicitly rejected in *GTE Sylvania* . . . as it had to be, since a horizontal agreement to divide territories is *per se* illegal . . . while *GTE Sylvania* held that a vertical agreement to do so is not.

Business Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 734 (1988) (citations omitted); see also Liebler, *supra* note 36, at 906-08 (stating that the *Sharp* Court's reaffirmation of the horizontal/vertical dichotomy represented an unfortunate reversion to a formalistic standard.)

213 769 F. Supp. 1506 (D. Minn. 1991).

214 *Id.* at 1517. The Court in *Lovett* was able to characterize the termination as horizontal under *Sharp* because it was induced by several distributors. *Id.* In *Big Apple BMW, Inc. v. BMW of North America, Inc.*, 1992-2 Trade Cas. (CCH) ¶ 69,918 (3d Cir. Aug. 6, 1992), the United States distributor for BMW automobiles had allegedly denied the plaintiff's BMW dealership application because of pressure from several other dealers who would have competed with the plaintiff. *Id.* at 68,389. The court concluded that, under *Sharp*, the dealers' group action should be characterized as a per se illegal horizontal restraint rather than as a vertical restraint subject to the rule of reason. *Id.* at 68,401-02. Similarly, in *ES Development, Inc. v. RWM Enterprises, Inc.*, 1991-2 Trade Cas. (CCH) ¶ 69,505 (8th Cir. 1991), *cert. denied*, 112 S. Ct. 1176 (1992), several automobile dealers had requested a group of manufacturers to refuse to franchise several other dealers at a nearby location. *Id.* at 66,198-200. In applying the per se rule, the court concluded that *Sharp* required that a more stringent standard be applied to horizontal than to vertical

It is more difficult to reconcile *Eastman Kodak* with *Sharp* in those cases in which only a single distributor convinces a supplier to terminate a rival. The *Sharp* Court found Business Electronics' termination to be vertical because one competitor rather than several had issued an ultimatum to Sharp.²¹⁵ Although this pedantic distinction bears no relationship to economic effect, the *Sharp* Court was clear in its requirement that the rule of reason should apply in single inducement cases.²¹⁶ The Court, however, did not specify how the rule of reason analysis should be conducted. The horizontal/vertical analysis proposed in this Article could qualify as the type of rule of reason approach mandated by *Sharp* for single inducement cases. Applying this approach to all horizontally induced terminations, regardless of the number of instigating distributors, would create an appropriate synthesis between *Sharp* and *Eastman Kodak* for the analysis of all mixed terminations. Under such an approach, the type of analysis employed by the courts would no longer turn on formalistic distinctions between "single" and "multiple" inducements of a distributor's termination.

In order to adopt this new approach, the courts must abandon their traditional view of the per se rule and the rule of reason as entirely divergent forms of antitrust analysis.²¹⁷ Indeed, it is more appropriate to view these two forms of analysis as parts of a continuum rather than as opposing approaches to antitrust analysis.²¹⁸ The objective of both types of analysis is to determine the likely competitive purpose and effect of the conduct in question. The rules differ only in the degree of inquiry necessary for the courts to feel comfortable that they have made such a determination effectively. The per se rule is simply a short-hand method by which the courts can assume the anticompetitive purpose and effect of conduct with which they are familiar.²¹⁹ The rule of reason requires a more detailed inquiry into particular conduct for which the competitive consequences are not as obvious.

conspiracies. *Id.* at 66,200-01.

215 *Sharp*, 485 U.S. at 734.

216 *Id.* at 726-31.

217 See *supra* notes 19-24 and accompanying text.

218 See Thomas A. Piraino, Jr., *Reconciling the Per Se and Rule of Reason Approaches to Antitrust Analysis*, 64 S. CAL. L. REV. 685 (1991).

219 See Herbert Hovenkamp, *Antitrust Policy, Restricted Distribution, and the Market for Exclusionary Rights*, 71 MINN. L. REV. 1293, 1294-95 n.8 (1987); Marks & Jacobson, *supra* note 142, at 211-12.

The rule of reason itself is not a unitary standard but encompasses varying degrees of inquiry. Although courts and commentators have traditionally believed that the approach requires an inquiry into all the relevant circumstances of a particular restraint,²²⁰ the courts in recent years have begun to apply more abbreviated versions of the rule of reason in certain circumstances. These new approaches recognize that often it is not practical, or desirable, for the fact finder to consider every factor that might conceivably bear on the competitive effect of the defendant's conduct.²²¹ One commentator has even concluded that in some cases the rule of reason can be applied in the "twinkling of an eye."²²² Thus, when the per se rule is inapplicable, the alternative need not be a full-blown analysis of the market impact of the restraint at issue.²²³

In a few recent cases, the Supreme Court has implicitly adopted a new intermediate rule of reason standard that focuses on a defendant's purpose for a restriction rather than on its market power.²²⁴ Eschewing a market analysis, the Court was willing to

220 See *supra* note 20 and accompanying text.

221 It is particularly difficult for the courts to define the relevant product and geographic markets and the defendant's relative share of those markets. Proving such issues requires extensive documentary evidence and endless testimony from economists and other experts. See Phillip Areeda, *The Changing Contours of the Per Se Rule*, 54 ANTITRUST L.J. 27, 28 (1985). Because the traditional rule of reason puts so many factors at issue, it is impossible to predict the outcome of cases. Indeed, one commentator recently described the traditional rule of reason analysis as "effectively worthless." Burns, *supra* note 75, at 37-38. Some courts have recently attempted to refine the rule of reason by adopting a "market power screen" for vertical restraints. Under this approach a vertical restriction cannot be found illegal unless a defendant possesses a market share above a particular threshold. See, e.g., *Assam Drug Co. v. Miller Brewing Co.*, 798 F.2d 311 (8th Cir. 1986); *Roland Mach. Co. v. Dresser Indus., Inc.*, 749 F.2d 380 (7th Cir. 1984); *Muenster Butane, Inc. v. Stewart Co.*, 651 F.2d 292, 298 (5th Cir. 1981); *O.S.C. Corp. v. Apple Computer, Inc.*, 601 F. Supp. 1274, 1291 n.8 (C.D. Cal. 1985), *aff'd*, 792 F.2d 1464 (9th Cir. 1986). The market power screen, however, still requires the courts to consider the defendant's market share, which is the most difficult factor in the rule of reason test. One commentator has thus concluded that "a market-share test would offer little help in determining the competitive effects of vertical restraints." William S. Comanor, *Vertical Price-Fixing, Vertical Market Restrictions and the New Antitrust Policy*, 98 HARV. L. REV. 983, 1001 n.81 (1985). The market power screen also disregards the impact of a vertical restraint on intrabrand competition. Even if a supplier has only a small share of the interbrand market, its termination of a distributor as a result of a competitor's inducement unreasonably restricts intrabrand competition.

222 Areeda, *supra* note 221, at 28.

223 See *infra* notes 236-49 and accompanying text.

224 See *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447 (1986); *NCAA v. Board of Regents*, 468 U.S. 85 (1985); *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679 (1978).

prohibit the restraints at issue simply because they had no valid competitive purpose. Such an approach is well suited to mixed terminations, where the supplier's motive for a termination is so revealing of its competitive effect.²²⁵ In *National Society of Professional Engineers v. United States*,²²⁶ an engineering society had prohibited competitive bidding by engineering contractors. In its opinion, the Court followed neither a traditional per se nor a standard rule of reason analysis. Instead of finding the ban on competitive bidding illegal on its face, the Court considered the defendants' arguments that the ban was necessary for public safety.²²⁷ However, at the same time, the Court completely avoided an analysis of the defendants' market power, prohibiting the ban on the simple grounds that it had no valid economic purpose.²²⁸ Similarly, in *NCAA v. Board of Regents*,²²⁹ the Court declined to apply a per se analysis to the NCAA's television restrictions. The NCAA had regulated the number of times its member colleges could appear on television and the amount they could be paid for such appearances.²³⁰ As in *Professional Engineers*, the Court did not require an analysis of specific competitive effects as an alternative to the per se rule.²³¹ The Court found the NCAA's restrictions to be illegal simply because they were not necessary to promote the NCAA's valid purpose of regulating amateur collegiate athletics.²³² Finally, in *FTC v. Indiana Federation of Dentists*,²³³ a dentists' association argued that it had refused to supply x-rays to insurance companies in order to enhance the quality of patient care. The Court refused to take a traditional per se approach to this group boycott.²³⁴ However, despite its avoidance of the per se rule, the Court found the conduct illegal after a rather abbreviated analysis indicated that there was no valid economic purpose for the refusal to supply the x-rays.²³⁵

225 See *supra* notes 128-44 and accompanying text.

226 435 U.S. 679 (1978).

227 *Id.* at 687-96.

228 *Id.* at 693 ("On its face, this agreement restrains trade within the meaning of § 1 of the Sherman Act.").

229 468 U.S. 85 (1985).

230 *Id.* at 91-94.

231 *Id.* at 86 ("[A]bsence of proof of market power does not justify a naked restriction on price or output") (syllabus).

232 *Id.* at 104-20.

233 476 U.S. 447 (1986).

234 *Id.* at 458.

235 *Id.* at 459-60 ("Application of the Rule of Reason to these facts is not a matter of

Consistent with the Court's approach in *Professional Engineers, NCAA*, and *Indiana Federation of Dentists*, the alternative to the per se rule in mixed termination cases need not be a full rule of reason market analysis. The courts can use an intermediate standard that considers the supplier's purpose for the termination. The but for causal analysis proposed in this Article is just such an intermediate standard. The analysis lies between the traditional per se rule and a typical rule of reason approach on the continuum of antitrust analysis. In contrast to a per se analysis, a supplier will have an opportunity to prove that it had a valid procompetitive purpose for a termination. Furthermore, unlike traditional rule of reason cases, a plaintiff would only have to show that a supplier had an improper purpose in order to prevail. Once a plaintiff meets the but for standard, it would not have to prove that the supplier possessed undue market power or that the termination unduly injured competition in the interbrand market.²³⁶

There is, in fact, specific Supreme Court authority for applying such a new rule of reason standard to mixed terminations. *Sylvania* is the only Supreme Court case that has indicated how a rule of reason analysis of nonprice vertical restrictions should be conducted.²³⁷ *Sharp* held that the termination of a distributor at the instigation of a single competitor was a nonprice vertical restraint.²³⁸ Thus, under *Sharp*, it is appropriate to apply the *Sylvania* balancing test to such a termination.

The *Sylvania* Court recognized that the reduction of intrabrand competition caused by vertical restrictions was justified by the corresponding stimulation of interbrand competition.²³⁹ Under *Sylvania*, therefore, the legality of a particular vertical restraint is determined by balancing any harm to intrabrand competition against the benefit to interbrand competition.²⁴⁰

any great difficulty [T]he Commission's failure to engage in detailed market analysis is not fatal to its finding of a violation").

236 Such a showing would be impossible for most terminated distributors. See *supra* notes 21, 44, 200 and accompanying text.

237 *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977).

238 *Business Elecs. Corp. v. Sharp Elecs. Corp.*, 485 U.S. 717, 723-31 (1987).

239 *Sylvania*, 433 U.S. at 54-55.

240 *Id.* at 57 n.27. Although *Sylvania* only referred to the balancing test in a cursory manner, nearly all courts and commentators have construed *Sylvania* to require such an approach. See, e.g., *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 745 (7th Cir. 1982); *Muenster Butane, Inc. v. Stewart Co.*, 651 F.2d 292, 296 (5th Cir. 1981); *Eiberger v. Sony Corp. of Am.*, 622 F.2d 1068, 1076 (2d Cir. 1980); Rozkowski, *supra*

The horizontal/vertical dichotomy fits perfectly with the *Sylvania* balancing test. As the Court stated in *Sylvania* and *Sharp*, interbrand competition is more important than intrabrand competition.²⁴¹ Thus, when a supplier independently acts to terminate a distributor, its natural intent to promote its interbrand competitiveness should be sufficient to outweigh any reduction of intrabrand competition resulting from the termination. However, when another distributor induces a termination, there is no beneficial interbrand effect to weigh in the balancing analysis. In such a case, the restriction of intrabrand competition alone justifies voiding the termination under a *Sylvania* balancing approach.²⁴² Such an analysis is consistent with *Eastman Kodak*, where the Court was concerned with efforts by firms to suppress competition from their intrabrand rivals.²⁴³

Once the horizontal or vertical origin of a termination is established, a court need not determine the parties' market power. Vertically imposed terminations should be allowed regardless of

note 83, at 157-58. The *Sylvania* balancing test has been criticized. One commentator has stated that it is "utterly incapable of principled judicial application." Rozkowski, *supra* note 83, at 158.

241 *Sharp*, 485 U.S. at 726; *Sylvania*, 433 U.S. at 52 n.19.

242 Several courts have held that the restriction of intrabrand competition, in the absence of a countervailing interbrand benefit, suffices to prove the illegality of a vertical restraint under the *Sylvania* balancing test. See *Sharp*, 485 U.S. at 749 (Stevens, J., dissenting) ("Not a word in the *Sylvania* opinion implied that the elimination of intrabrand competition could be justified as reasonable without any evidence of a purpose to improve interbrand competition."); *Com-Tel, Inc. v. DuKane Corp.*, 669 F.2d 405, 412 (6th Cir. 1982) (stating that "appellants' conduct not only reduced intrabrand competition but also did not promote interbrand competition"); *Eiberger v. Sony Corp. of Am.*, 622 F.2d 1068, 1075, 1081 (2d Cir. 1980) (indicating that in cases in which no interbrand benefit is established, an adverse impact on intrabrand competition alone may support a finding of an antitrust violation); see also *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 459 (1986) ("Absent some countervailing procompetitive virtue[,] . . . an agreement limiting consumer choice . . . cannot be sustained under the Rule of Reason."). Some courts and commentators, however, believe that the mere restriction of intrabrand competition is not sufficient to prove the illegality of a vertical restraint and that, in addition, the plaintiff must prove an adverse effect on interbrand competition. See *Murphy v. Business Cards Tomorrow, Inc.*, 854 F.2d 1202, 1205 (9th Cir. 1988) ("[T]he effect on intrabrand competition 'is not relevant if there is intense interbrand competition.'") (quoting the lower court); *Crane & Shovel Sales Corp. v. Bucyrus-Erie Co.*, 854 F.2d 802 (6th Cir. 1988) (adverse effect on intrabrand competition resulting from termination of several dealers insufficient to support illegality); *Tunis Bros., Inc. v. Ford Motor Co.*, 952 F.2d 715 (3d Cir. 1991) (termination of dealer not illegal because interbrand competition unaffected); *Westman Comm'n Co. v. Hobart Int'l, Inc.*, 796 F.2d 1216 (10th Cir. 1986) (same); *Ron Tonkin Gran Turismo, Inc. v. Fiat Distribs., Inc.*, 637 F.2d 1376 (9th Cir. 1981) (same).

243 See *supra* notes 205-11 and accompanying text.

the manufacturer's size, while horizontally motivated terminations should be illegal even when they are induced by small distributors. A termination effected independently by a supplier is no less ancillary to a procompetitive purpose simply because the supplier happens to have a large market share. Large manufacturers should be just as motivated as smaller ones to ensure that their distribution systems deliver products to consumers in the most efficient manner.²⁴⁴ Furthermore, an induced termination is no less restrictive of intrabrand competition when the supplier has a small share of the interbrand market or the terminated dealer has a small business. In fact, the smaller dealer is more likely to be on the receiving end of a termination induced by a larger competitor. The harm to intrabrand competition is particularly significant in such a case because the small entrepreneur is often the most innovative deliverer of services to consumers and the greatest impetus to the efficiency of competing dealers.²⁴⁵

The courts have defined market power as "the power to control prices or exclude competition."²⁴⁶ When the but for test is met, a dealer clearly has exercised the power to exclude a competitor from the relevant market. Thus, no further proof of the defendant's market power should be necessary.²⁴⁷ When a

244 The *Sylvania* Court relied on the fact that the presence of interbrand competition would act as a natural check on manufacturers' limitation of intrabrand competition. *Sylvania*, 433 U.S. at 56. It could be argued that monopolists who face no interbrand competition would not be restrained in limiting the adverse competitive effects of distributor terminations and, therefore, that terminations independently effected by monopolists should not always be upheld. There is some precedent for finding vertical restrictions illegal when they are imposed by manufacturers with market shares in excess of 70%. See *Graphic Prods. Distribs., Inc. v. Itek Corp.*, 717 F.2d 1560 (11th Cir. 1983). As some commentators have pointed out, however, even monopolists want to produce a product mix at a resale level that is attractive to consumers and thus would be no less interested than nonmonopolists in ensuring the efficiency of vertical restrictions. See also Wesley J. Liebler, *Intrabrand "Cartels" Under GTE Sylvania*, 30 UCLA L. REV. 1, 26 n.78 (1982); Panel Discussion, *Counseling Your Client on Horizontal and Vertical Restraints*, 55 ANTITRUST L.J. 293, 307 (1986) (comments of Donald F. Turner, member of the District of Columbia Bar).

245 As one commentator has stated: "[G]iven that boycotts historically have been the favored weapon of retailers in suppressing the competition provided by more efficient discounters, any use of the tactic against discounters should be condemned under the antitrust laws as a prophylactic measure." Gerla, *supra* note 44, at 11. Also, as the Supreme Court stated in *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1958), such a termination "is not to be tolerated merely because the victim is just one merchant whose business is so small that his destruction makes little difference to the economy. Monopoly can as surely thrive by the elimination of such small businessmen, one at a time, as it can by driving them out in large groups." *Id.* at 213 (footnote omitted).

246 See *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 391 (1956).

247 In *Eastman Kodak*, the Supreme Court was willing to infer Kodak's power in the

defendant's conduct has such a clear anticompetitive effect and is so devoid of any redeeming competitive virtue, there is nothing to gain—and much to lose—by requiring a plaintiff to meet the difficult burdens of a market power inquiry.²⁴⁸

Dispensing with a market power analysis would simplify mixed termination cases considerably and provide clearer guidance on what conduct is acceptable. Regardless of their size, manufacturers would feel free to proceed with terminations designed to make themselves more effective competitors in the interbrand market. At the same time, suppliers and dealers would know that all induced terminations would be deemed illegal on their face. Under such a clear standard, distributors would be deterred from attempting to induce a competitor's termination. Manufacturers could readily resist such inducement by informing the complaining dealer that both parties would risk liability under the Sherman Act if the manufacturer proceeded with the termination.²⁴⁹

VIII. CONCLUSION

Mixed termination cases can be analyzed in a way that effectively reveals whether their substantive competitive effect is horizontal or vertical. In contrast to the extreme approaches recently taken by Congress and many federal courts, a horizontal/vertical dichotomy fairly balances the interests of suppliers and terminated distributors. This approach avoids both the harshness of the per se rule and the weakness of the traditional rule of reason. By separating the issue of the cause of a termination from the issue of conspiracy, the courts can focus on the parties' purpose for a mixed termination. This new intermediate standard is consistent with *Sylvania's* requirement that antitrust rules be based on demonstrable economic effect and with *Sharp's* disavowal of a tradi-

photocopier parts market from its ability to drive independent service organizations out of business. *Eastman Kodak Co. v. Image Technical Servs.*, 112 S. Ct. 2072, 2080-81 (1992). As the Court stated, "It is clearly reasonable to infer that Kodak has market power to raise prices and drive out competition in the aftermarkets, since respondents offer direct evidence that Kodak did so." *Id.* at 2088.

248 As Professor Areeda has stated, "Once we decide that a class of practice is in the vast generality of cases detrimental and unjustified, why bother with the complicated and expensive inquiry into power?" Areeda, *supra* note 21, at 28.

249 The deterrent effect of the analysis proposed in this Article would be similar to the approach adopted by Congress in the Robinson-Patman Act, under which it is illegal not only for a supplier to engage in price discrimination but also for a buyer to knowingly induce the grant of a discriminatory discount. See 15 U.S.C. § 13(f) (1988).

tional per se analysis for terminations induced by a single distributor. The new standard is also in accordance with the Supreme Court's recent recognition in *Eastman Kodak* of the need to prevent the unjustified exclusion of competitors from intrabrand markets. The federal courts are thus free to adopt the approach under current Supreme Court standards. By doing so, they may convince Congress to abstain from ill-conceived legislation to alter the judicial approach to mixed terminations.